NOTE

This Microfiche meets the quality requirements of the American National Standard for Microfiche of Documents (ANSI PH5.9-1975). However, because of imperfections in the document from which it was made, it contains images that are illegible or difficult to read. The source document for this microfiche is the best copy that could be obtained prior to filming.

CIS

Congressional Information Service, Inc
Washington, D.C.

S. HRG. 101-765

TELEMARKETING AND CONSUMER FRAUD

HEARING

BEFORE THE

SUBCOMMITTEE ON THE CONSUMER

OF THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION
UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

SECOND SESSION

ON

S. 1441

TO ENHANCE THE FEDERAL TRADE COMMISSION'S ABILITY TO PREVENT CONSUMER FRAUD

S. 2494

TO STRENGTHEN THE AUTHORITY OF THE FEDERAL TRADE COMMISSION REGARDING FRAUD COMMITTED IN CONNECTION WITH SALES MADE WITH A TELEPHONE, AND FOR OTHER PURPOSES

MAY 2, 1990

Printed for the use of the
Committee on Commerce, Science, and Transportation

U.S. GOVERNMENT PRINTING OFFICE
31-349 O WASHINGTON : 1990

S261-71

For sale by the Superintendent of Documents, Congressional Sales Office
U.S. Government Printing Office, Washington, DC 20402

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

ERNEST F. HOLLINGS, South Carolina, *Chairman*

DANIEL K. INOUYE, Hawaii
WENDELL H. FORD, Kentucky
J. JAMES EXON, Nebraska
ALBERT GORE, JR., Tennessee
JOHN D. ROCKEFELLER IV, West Virginia
LLOYD BENTSEN, Texas
JOHN F. KERRY, Massachusetts
JOHN B. BREAUX, Louisiana
RICHARD H. BRYAN, Nevada
CHARLES S. ROBB, Virginia

JOHN C. DANFORTH, Missouri
BOB PACKWOOD, Oregon
LARRY PRESSLER, South Dakota
TED STEVENS, Alaska
ROBERT W. KASTEN, JR., Wisconsin
JOHN McCAIN, Arizona
CONRAD BURNS, Montana
SLADE GORTON, Washington
TRENT LOTT, Mississippi

KEVIN G. CURTIN, *Chief Counsel and Staff Director*
WALTER B. MCCORMICK, JR., *Minority Chief Counsel and Staff Director*

SUBCOMMITTEE ON THE CONSUMER

RICHARD H. BRYAN, Nevada, *Chairman*

ALBERT GORE, JR., Tennessee
WENDELL H. FORD, Kentucky
CHARLES S. ROBB, Virginia

SLADE GORTON, Washington
JOHN McCAIN, Arizona
ROBERT W. KASTEN, JR., Wisconsin

CONTENTS

Page
Opening statement by Senator Bryan 1
Opening statement by Senator McCain 2
Text of bills:
- S. 1441 5
- S. 2494 17

LIST OF WITNESSES

Barton, Richard A., senior vice president, government affairs, Direct Marketing Assn 71
- Prepared statement 74

Collier, Richard, director, special projects, MasterCard International, Inc 86
- Prepared statement 89

King, Jane, on behalf of the National Association of Consumer Agency Administrators 69
Luken, Hon. Thomas A., U.S. Representative from Ohio 30
McKay, Brian, on behalf of the National Association of Attorneys General 63
Santini, James D., Washington DC representative of the National Tour Assn 110
Steiger, Hon. Janet, Chairman, FTC; accompanied by Barry Cutler, Director, Bureau of Consumer Protection 33
- Prepared statement 37

ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

Association of National Advertisers, Inc., statement 145
Barrett, Dr. Stephen, consumer advocate, letter 133
Eggleston, Fred, Deputy General Counsel, U.S. Postal Service, letter 140
Eikenberry, Ken, Washington State attorney general, statement 154
Gilmore, Voit, president and CEO, American Society of Travel Agents, letter 135
National Consumers League, statement 174
Steiger, Hon. Janet D., Chairman, FTC, letter 119
Strenio, Andrew J., Jr., Member, FTC, letter 137
VISA U.S.A., Inc. and MasterCard International, Inc., statement 160

TELEMARKETING AND CONSUMER FRAUD

WEDNESDAY, MAY 2, 1990

U.S. SENATE,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
SUBCOMMITTEE ON THE CONSUMER,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:34 a.m., in room 253, Russell Senate Office Building, Hon. Richard H. Bryan [chairman of the subcommittee] presiding.

Staff members assigned to this hearing: Linda Lance and Moses Boyd, staff counsels and Sherman Joyce, minority staff counsel.

OPENING STATEMENT BY SENATOR BRYAN

Senator BRYAN. Good morning. This morning, the Consumer Subcommittee will consider the issue of consumer fraud, and particularly fraud carried out through the use of the telephone.

As we all know, telephone sales are increasingly being used by both legitimate businesses for consumer convenience and by those who are out to defraud and harass the public. More than $100 billion in sales are estimated to be made by telephone each year. Unfortunately, estimates of the annual cost of fraudulent sales now range in the $1 billion figure.

No one is more aware of this than the citizens of my own home State of Nevada. Last summer, the subcommittee held its first hearing on this issue and focused on penny stock fraud in Las Vegas and heard some rather memorable testimony from consumers about fraudulent schemes practiced in the Southern Nevada area.

In fact, it is fair to say that during the 1980s, fraudulent telemarketing boiler rooms were a growth industry in Nevada. The State's Consumer Affairs Division has records of more than 15,000 written complaints and more than 66,000 inquiries from consumers concerned about such fraud. It is estimated that in Nevada alone, consumers lost more than $8 million between 1984 and 1989 because of fraudulent telemarketing schemes.

State government, together with the Federal strike force, has done an admirable job in attempting to deal with this overwhelming problem. The boiler-room industry has gone into sharp decline, from more than 400 telemarketing firms with 20,000 employees in 1988 to 60 operations with 5,000 sales representatives in 1989.

Additionally and parenthetically, I might note that there have been 100 convictions by those who have been involved in perpetrating telemarketing fraud in my own State. The State has enacted an effective and comprehensive legislative program to address this problem, which among other things, requires the licensing of telemarketing and establishment of tough anti-fraud provisions in the securities area.

Despite these noteworthy efforts the problem has not been eliminated, either in Nevada or in the rest of the country. The legislation which I have introduced and is the subject of this hearing, together with legislation that Senator McCain has introduced, represent efforts towards maximizing the efforts at the Federal level to protect consumers from being swindled out of money which they cannot afford to lose.

Legislation in this area must be carefully crafted to avoid unduly burdening the many legitimate telemarketers and to find the proper balance between Federal and State enforcement roles. I believe that the bill which I have crafted accomplishes those goals and will effectively address this problem. However, I look forward to the testimony of our witnesses this morning, which I believe will be of great assistance to the Subcommittee in ensuring the effectiveness of legislation which may be processed by the Committee.

I am particularly pleased this morning that we will be hearing from Chairman Steiger of the Federal Trade Commission and Attorney General Bryan McKay from my own State of Nevada. I know that Chairman Steiger has had a grueling schedule of hearings both in the Senate and the House this week, and I very much appreciate her taking time out of her own busy schedule to join us here today. Her presence is reflective of the priority the Federal Trade Commission places on this important consumer issue, and I look forward to working with her and the Commission as we seek to find a solution to this problem.

I also note the appearance this morning of Attorney General Bryan McKay, who has been on the front lines of our efforts in Nevada to combat telemarketing fraud. His presence this morning comes at no little inconvenience to him. Having made that trip a number of times myself, Attorney General McKay, I appreciate, as does the Subcommittee, your presence here as well.

We have been joined on the Subcommittee this morning by Senator John McCain, who himself has a piece of legislation which is the subject of this hearing and who has long been interested in this area and like I seeks a legislative response crafted to addressing the appropriate Federal role in telemarketing fraud.

Senator McCain I defer to you now, sir.

OPENING STATEMENT BY SENATOR McCAIN

Senator McCain. Thank you very much, Mr. Chairman, and I want to commend you not only for holding this hearing today but for all of the efforts you have made on behalf of consumers who are being mistreated and exploited in various ways. This issue is a problem that is growing, and one that I know we both find especially troublesome.

The cost of fraud to the American consumer is nothing short of staggering. Billions of dollars are lost to scam artists every year, but the cost cannot only be measured in dollars. There is human cost as well. People's health and well-being have been endangered by bogus health products and services like phony vitamins, weight loss plans, baldness remedies and cancer cures.

The types of fraud that are perpetrated on the American public are limited only by the imagination of clever con artists. People in telemarketing boiler rooms pedal worthless gem stones, gold mines or vacation packages. Health quacks pedal new cures for Alzheimer's Disease or impotence. Organizations claiming to be advocates for the interests of older Americans send mailings to seniors that are deceptively official-looking in an attempt to pry away some or all of their fixed income.

Mr. Chairman, there can be little question that this country is facing a fraud problem of tremendous and growing proportions. In my State of Arizona alone, for example, the Attorney General's Office has reported that complaints about fraudulent contests have increased from 334 in 1988 to almost 2,500 expected by the end of this year.

One Arizona company sold millions of dollars worth of a diet pill called "Dream Away" that, if taken at bedtime, promised to make you lose weight without sleeping. No dieting or exercising was required. They charged people $19.95 for a 21-day supply of these pills, which turned out to be nothing more than small amounts of amino acids found in everyone's ordinary diet.

Another company that operated a mine in Arizona promised its unsuspecting investors gold and silver at low prices from a mine site that had no gold or silver reserves.

Health fraud alone is big business in this country. Estimates are that Americans spend about $27 billion a year on quack products or treatments. The Food & Drug Administration estimates that 38 million Americans have used a fraudulent health product within the past year, and one out of ten of those people was harmed by side effects.

When it comes to swindling people, scam artists are not particularly discriminating. They prey on people of all ages, of all income levels and with all levels of education. A particularly vulnerable group of consumers, though, is the elderly. The House Select Committee on Aging found that seniors are the most affected by quackery.

For a variety of reasons, advancing age seems to bring with it an increased vulnerability to crimes such as fraud. For one, seniors are major consumers of services and products targeted by con artists. Illnesses or diseases suffered by seniors may make wonder cures very enticing. For another, seniors have fixed incomes which make get-rich-quick schemes all the more attractive.

While fraud is not confined to older Americans, it is often successful amongst this group, especially with those who live alone, are lonely, or who may have recently suffered the loss of someone close.

I represent a State, as you do, Mr. Chairman, which has a considerable number of older Americans. I have seen the magnitude of fraudulent practices targeted against our seniors. As a result, I introduced S. 1441, the Consumer Fraud Prevention Act, a bill that would strengthen the Federal Trade Commission's ability to fight against all types of consumer fraud perpetrated not only against older Americans but against all Americans.

One major problem in combating consumer fraud has been the jurisdictional restraints on the FTC's law enforcement activities. Many scam artists operate out of so-called boiler-rooms, consisting of nothing more than banks of phone lines with solicitors making calls to unsuspecting prospects. This type of operation makes victims hard to locate and evidence hard to come by.

On top of those frustrations, once the scam operators think that legal action by the authorities is imminent, they simply pack up and move across State lines, making law enforcement more difficult. The legislation I have introduced would give the FTC broader and more effective tools to pursue all types of consumer fraud.

Mr. Chairman, I know that you have had a longstanding concern about this issue and have recently introduced a bill to address the problem of telemarketing fraud. Our bills differ some in approach. Both bills reflect the belief that current enforcement authority is not sufficient to swiftly and effectively deal with those who defraud the American consumer.

With respect to scope, both bills deal with telemarketing. Mine, however, goes beyond telemarketing to cover other important areas of consumer fraud such as health care quackery and fraud in the life care industry.

I look forward to hearing from today's witnesses on how best to fix this vexing problem of consumer fraud, and I look forward, Mr. Chairman, to combining efforts with you to come up with a good piece of legislation that we can report out of this Subcommittee and out of the Committee.

[The bills follow:]

II

101st CONGRESS
1st Session

S. 1441

To enhance the Federal Trade Commission's ability to prevent consumer fraud.

IN THE SENATE OF THE UNITED STATES

July 31 (legislative day, January 3), 1989

Mr. McCain introduced the following bill; which was read twice and referred to the Committee on Commerce, Science, and Transportation

---

A BILL

To enhance the Federal Trade Commission's ability to prevent consumer fraud.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Consumer Fraud Prevention Act".

FINDINGS

Sec. 2. The Congress finds that:

(1) Consumer fraud is a pervasive and persistent problem for American businesses and consumers;

(2) Consumer fraud costs Americans billions of dollars each year, and it undermines legitimate com-

mercial activities by businesses of all sizes and in all fields.

(3) Consumer fraud schemes commonly exceed the jurisdictional boundaries of any single court or State.

(4) The perpetrators of consumer fraud use various means to escape prosecution, including rapid flight, jurisdictional diversity, and fictitious legal entities.

(5) One of the most pervasive types of consumer fraud is health fraud, which has been estimated to cost Americans more than $10,000,000,000 annually. In addition to being costly, such fraud can be life threatening.

(6) Consumer fraud involving telemarketing is estimated to cost consumers billions of dollars annually. Telemarketing involving investment fraud alone is estimated to cost $1,000,000,000 each year.

(7) The Federal Trade Commission and the attorneys general of the States have initiated a cooperative attack on telemarketing fraud. The success of this program has been hampered by jurisdictional limitations and inadequate resources.

(8) Consumer fraud is a particular burden for senior citizens, who are more frequently defrauded than other consumers.

(9) The ability of the Federal Trade Commission to attack consumer fraud has been limited due to inadequate authority, and legislation is needed to enhance the Commission's ability to protect consumers from such abuses.

FALSE ADVERTISEMENTS CONCERNING SERVICES

SEC. 3. Section 12(a) of the Federal Trade Commission Act (15 U.S.C. 52(a)) is amended by inserting "services," immediately after "devices," each place it appears.

EXPANDED ENFORCEMENT TOOLS

SEC. 4. (a) VENUE.—(1) Subsections (a) and (b) of section 13 of the Federal Trade Commission Act (15 U.S.C. 53) are each amended by adding at the end thereof the following: "Whenever it appears to the court that the interests of justice require that any other person, partnership, or corporation should be a party in such suit, the court may cause such person, partnership, or corporation to be summoned whether or not they reside or transact business in the district in which the suit is brought, and to that end process may be served in any district.".

(2) Section 13 of the Federal Trade Commission Act (15 U.S.C. 53) is amended by redesignating subsection (c) as subsection (d) and inserting immediately after subsection (b) the following:

"(c) Any process of the Commission under this section may be served by anyone duly authorized by the Commission—

"(1) by delivering a copy of such process to the person to be served, to a member of the partnership to be served, or to the president, secretary, or other executive officer or a director of the corporation to be served;

"(2) by leaving a copy of such process at the residence or the principal office or place of business of such person, partnership, or corporation; or

"(3) by mailing a copy of such process by registered mail or certified mail addressed to such person, partnership, or corporation at his or her or its residence or principal office or place of business.

The verified return by the person so serving such process setting forth the manner of such service shall be proof of the same, and the return post office receipt for such process mailed by registered mail or certified mail as provided in this subsection shall be proof of the service of the same.".

(b) SUBPOENA.—(1) Section 20(a) of the Federal Trade Commission Act (15 U.S.C. 57b–1(a)) is amended by redesignating paragraph (7) as paragraph (8) and inserting after paragraph (6) the following:

"(7) The term 'physical evidence' means any object or device including any medical device, food product, drug, nutritional product, cosmetic product, or audio or video recording.".

(2) Section 20(c)(1) of the Federal Trade Commission Act (15 U.S.C. 57b–1(c)(1)) is amended—

(A) by inserting "physical evidence or" immediately after "any" the second time it appears;

(B) by inserting "to produce such physical evidence for inspection," immediately before "to produce";

(C) by inserting "physical evidence," immediately after "concerning"; and

(D) by inserting "evidence," immediately before "material, answers,".

(3) Section 20(c)(3) of the Federal Trade Commission Act (15 U.S.C. 57b–1(c)(3)) is amended—

(A) by inserting "physical evidence or" immediately before "documentary material";

(B) in subparagraph (A)—

(i) by inserting "physical evidence or" immediately before "documentary"; and

(ii) by inserting "evidence or" immediately after "permit such";

(C) in subparagraph (B), by inserting "evidence or" immediately before "material"; and

(D) in subparagraph (C), by inserting "evidence or" immediately before "material".

(4) Section 20(c)(10) of the Federal Trade Commission Act (15 U.S.C. 57b-1(c)(10)) is amended by inserting "physical evidence or" immediately before "documentary material" each place it appears.

(c) POSTAL DATA.—Notwithstanding any other provision of law, the United States Postal Service shall, within 180 days after the date of enactment of this Act, amend its regulations in part 233 of title 39, Code of Federal Regulations, concerning mail covers to provide that the Federal Trade Commission may, in the course of investigating unfair or deceptive acts or practices in violation of section 5 of the Federal Trade Commission Act (15 U.S.C. 45), obtain access to mail cover reports to the same extent and in the same manner as law enforcement agencies investigating the commission or attempted commission of a crime.

(d) FINANCIAL DATA.—Section 1109(a)(3) of Public Law 95-360, approved November 10, 1978, is amended—

(1) by redesignating subparagraph (E) as subparagraph (F);

(2) in subparagraph (D), by striking "or"; and

(3) by inserting immediately after subparagraph (D) the following new subparagraph;

"(E) dissipation, removal, or destruction of assets that are subject to forfeiture, seizure, redress, or restitution under any law of the United States by reason of having been obtained in violation of law; or".

(e) ASSISTANCE OF STATE ATTORNEYS GENERAL.—(1) The Commission may appoint State attorneys general to assist Commission attorneys to enforce Commission rules when the public interest so requires. The Commission shall, within fifteen days after receiving any request from a State attorney general for such an appointment, determine whether to grant the request and communicate such determination to that State attorney general.

(2) Each person appointed under this subsection is subject to removal by the Commission at its discretion.

RULEMAKING ON TELEMARKETING

SEC. 5. (a) RULEMAKING.—Within two hundred and seventy days after the date of enactment of this Act, the Federal Trade Commission shall amend its rule in part 435 of title 16, Code of Federal Regulations, concerning mail order merchandise, to apply also to telemarketing. Except as specified in the remainder of this subsection, the amended rule shall apply to telemarketing to the same extent and in the same manner as it now applies to mail order sales.

(b) TELEMARKETING REQUIREMENTS.—As part of the rulemaking required by subsection (a) of this section the Commission shall consider including in the final rule a requirement that—

(1) each telemarketer shall inform the person, partnership, or corporation to whom the telemarketing is directed that such person, partnership, or corporation is entitled to a refund of any money paid for the product or service which is the subject of the telemarketing if delivery of the product or service is not made—

(A) within the time period included in the offer of the product or service, or

(B) if no time period is included in such offer, within thirty days after the date the offer is made; and

(2) if such telemarketer—

(A) makes an unsolicited telephone call to a person, partnership, or corporation or otherwise communicates with such person, partnership, or corporation offering a free gift or prize and invites such person, partnership, or corporation to respond,

(B) a specific product or service is offered or sold in connection with such telephone call or other communication, and

(C) there is no Federal statute governing such telephone call or other communication involving such product or service,

such person, partnership, or corporation may cancel an order for such product or service not later than the expiration of three days after the date on which there is a sales agreement.

(c) REBUTTABLE PRESUMPTION.—Such amended rule shall include a rebuttable presumption that if a telemarketer does not keep adequate records to show compliance with the requirements described in subsection (b) of this section, such telemarketer shall be considered to be in violation of such requirement.

(d) LIMITATION.—For purposes of this section, a financial institution or other participant in a payment system used to pay for products or services offered or sold through telemarketing, including the credit or payment authorization aspect of such payment system, is not, by virtue of such participation, a telemarketer nor a person, partnership, or corporation which acts in concert with, or on behalf of, a telemarketer.

(e) DEFINITIONS.—For purposes of this section—

(1) the term "telemarketer" means a person, partnership, or corporation which engages in telemarketing; and

(2) the term "telemarketing" means the use of a telephone in the ordinary course of business to communicate with a person, partnership, or corporation an offer for sale or to complete a sale of a product or service.

LIFE CARE HOME STUDY

SEC. 6. (a) STUDY.—The Federal Trade Commission shall conduct a study of unfair or deceptive acts or practices in the life care home industry, including acts or practices engaged in by life care homes. Within twenty-four months of the date of enactment of this section, the Commission shall report the findings and conclusions of the study to Congress. The Commission shall indicate in its report whether it intends to initiate a trade regulation rulemaking under section 18 of the Federal Trade Commission Act respecting unfair or deceptive acts or practices in the life care home industry and the reasons for such determination.

(b) DEFINITIONS.—For purposes of subsection (a):

(1) The term "life care home" includes the facility or facilities occupied, or planned to be occupied, by residents or prospective residents where a provider undertakes to provide living accommodations and services pursuant to a life care contract, regardless of whether such facilities are operated on a profit or nonprofit basis.

(2) The term "life care contract" includes a contract between a resident and a provider to provide the resident, for the duration of such resident's life, living accommodations and related services in a life care home, including nursing care services, medical services, and other health-related services, which is conditioned upon the transfer of an entrance fee to the provider and which may be further conditioned upon the payment of periodic service fees.

LONG-TERM HEALTH CARE INSURANCE STUDY

SEC. 7. (a) STUDY.—The Federal Trade Commission shall conduct a study concerning—

(1) the use of unfair or deceptive acts or practices in the marketing and sale of long-term health care policies to the elderly;

(2) the relationship of premiums for long-term health care policies to unexpected (expected) claims paid under such policies;

(3) the effectiveness of various alternatives supported by the States to prevent unfair or deceptive acts or practices in the marketing and sale of long-term health care policies for the elderly; and

(4) the ability of consumers to compare different long-term health care policies.

(b) REPORT.—The Commission shall, not later than one year after the date of enactment of this Act, report the results of the study conducted under subsection (a) to the Committee on Commerce, Science, and Transportation of the Senate and the Committee on Energy and Commerce of the House of Representatives.

(c) COMPTROLLER GENERAL.—In conducting the study under subsection (a), the Commission shall consult with the Comptroller General of the United States.

(d) DEFINITION.—For purposes of subsection (a), the term "long-term health care policy" includes any insurance policy which provides, among other benefits, a predetermined or fixed benefit payment for each day the policyholder stays in a nursing or care facility.

II

101st CONGRESS
2d Session

S. 2494

To strengthen the authority of the Federal Trade Commission regarding fraud committed in connection with sales made with a telephone, and for other purposes.

IN THE SENATE OF THE UNITED STATES

April 23 (legislative day, April 18), 1990

Mr. Bryan introduced the following bill; which was read twice and referred to the Committee on Commerce, Science, and Transportation

---

A BILL

To strengthen the authority of the Federal Trade Commission regarding fraud committed in connection with sales made with a telephone, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Telemarketing Fraud and Abuse Prevention Act of 1990".

DEFINITIONS

Sec. 2. As used in this Act, the term—

(1) "attorney general" means the chief legal officer of a State;

(2) "Commission" means the Federal Trade Commission;

(3) "State" means any State of the United States, the District of Columbia, Puerto Rico, the Northern Mariana Islands, and any territory or possession of the United States; and

(4) "telemarketing" means a plan, program, or campaign conducted to induce purchases of goods or services by significant use of one or more telephones through interstate voice telephone calls; the term does not include other use of a telephone in connection with business or personal transactions.

TELEMARKETING RULES

SEC. 3. (a) The Commission shall prescribe rules regarding telemarketing activities. In prescribing such rules, the Commission shall consider the inclusion of—

(1) a requirement that goods or services offered by telemarketing be shipped or provided within a specified period and that if the goods or services are not shipped or provided within such period a refund be required;

(2) authority for a person who orders a good or service through telemarketing to cancel the order within a specified period;

(3) restrictions on the hours of the day when unsolicited telephone calls can be made to consumers;

(4) a prohibition of telemarketing generated by computers on equipment that does not permit the individual called to terminate the telephone call immediately; and

(5) recordkeeping requirements.

(b) The Commission shall prescribe the rules under subsection (a) of this section within one hundred and eighty days after the date of enactment of this Act. Such rules shall be prescribed in accordance with section 553 of title 5, United States Code.

(c) Any person who violates any rule prescribed under subsection (a) of this section shall be considered to have engaged in an unfair or deceptive act or practice in or affecting commerce prohibited by section 5 of the Federal Trade Commission Act (15 U.S.C. 45).

(d) If, upon application to the Commission by an appropriate State agency, the Commission determines (pursuant to rules prescribed by the Commission) that—

(1) there is in effect a State requirement which applies to any telemarketing to which this section applies; and

(2) such State requirement affords an overall level of protection to consumers which is as great as, or greater than, the protection afforded by this section;

then only such State requirement shall be applicable to the extent specified in such determination for so long as the State administers and enforces effectively any such State requirement, as determined by the Commission.

ACTIONS BY STATE ATTORNEYS GENERAL

SEC. 4. (a)(1) Whenever it shall appear to the attorney general of any State that the interests of the residents of that State have been, are being, or may be threatened or adversely affected because any person has engaged, is engaging, or is about to engage in telemarketing which is a fraudulent act or practice or which violates any rule, regulation, or order of the Commission under this Act, the State may bring a civil action on behalf of its residents to enjoin such telemarketing, to enforce compliance with any rule, regulation, or order of the Commission under this Act, to obtain damages on behalf of their residents, or to obtain such further and other relief as the court may deem appropriate.

(2) The district courts of the United States, the United States courts of any territory, and the District Court of the United States for the District of Columbia shall have jurisdiction over all civil actions brought under this section to enforce any liability or duty created by any rule, regulation, or order of the Commission under this Act, or to obtain damages or other relief with respect thereto. Upon proper application, such courts shall also have jurisdiction to issue writs of mandamus, or orders affording like relief, commanding the de-

fendant to comply with the provisions of any rule, regulation, or order of the Commission under this Act, including the requirement that the defendant take such action as is necessary to remove the danger of violation of any such rule, regulation, or order. Upon a proper showing, a permanent or temporary injunction or restraining order shall be granted without bond.

(3) Immediately upon instituting any such civil action, the State shall serve written notice of the action upon the Commission and provide the Commission with a copy of its complaint, and the Commission shall have the right (A) to intervene in the action, (B) upon so intervening, to be heard on all matters arising therein, and (C) to file petitions for appeal.

(4) Any civil action brought under this section in a district court of the United States may be brought in the district wherein the defendant is found or is an inhabitant or transacts business or wherein the telemarketing occurred, is occurring, or is about to occur, and process in such cases may be served in any district in which the defendant is an inhabitant or wherever the defendant may be found.

(5) For purposes of bringing any civil action under this section, nothing in this Act shall prevent the attorney general from exercising the powers conferred on the attorney general by the laws of such State to conduct investigations or to ad-

minister oaths or affirmations or to compel the attendance of witnesses or the production of documentary and other evidence.

(6) Nothing contained in this section shall prohibit an authorized State official from proceeding in State court on the basis of an alleged violation of any general civil or criminal antifraud statute of such State.

(7) The State shall give the Commission prior written notice of its intent to proceed, before instituting a proceeding in State court as described in this subsection, and shall furnish the Commission with a copy of its complaint immediately upon instituting such proceeding. The Commission shall have the right (A) to intervene in the proceeding, (B) upon so intervening, to be heard on all matters arising therein, and (C) to file a petition for appeal. The Commission or the defendant may remove such proceeding to the district court of the United States from the proper district by following the procedure for removal otherwise provided by law, except that the petition for removal shall be filed within sixty days after service of the summons and complaint upon the defendant. The Commission shall have the right to appear as amicus curiae in any such proceeding.

ACTIONS BROUGHT BY PRIVATE PERSONS

SEC. 5. (a) As used in this section, the term "person adversely affected by telemarketing" includes a member organization comprised of financial institution members, or a parent organization of such member organization, if one or more of the financial institution members is eligible to bring a civil action under this subsection, and such term does not include a governmental entity.

(b)(1) Any person adversely affected by telemarketing which is a fraudulent act or practice or which violates any rule, regulation, or order of the Commission under this Act may bring a civil action against a person who has engaged, is engaging, or is about to engage in such telemarketing if the amount in controversy exceeds the sum or value of $50,000. Such an action may be brought to enjoin such telemarketing, to enforce compliance with any rule, regulation, or order of the Commission under this Act, to obtain damages on behalf of their residents, or to obtain such further and other relief as the court may deem appropriate.

(2) The district courts of the United States, the United States courts of any territory, and the District Court of the United States for the District of Columbia shall have jurisdiction over all civil actions brought under this section to enforce any liability or duty created by any rule, regulation, or order of the Commission under this Act, or to obtain damages or other relief with respect thereto. Upon proper application, such courts shall also have jurisdiction to issue writs of mandamus, or order affording like relief, commanding the defendant to comply with the provisions of any rule, regulation, or

order of the Commission under this Act, including the requirement that the defendant take such action as is necessary to remove the danger of violation or of any such rule, regulation, or order. Upon a proper showing, a permanent or temporary injunction or restraining order shall be granted without bond.

(3) Immediately upon instituting any such civil action, the plaintiff shall serve written notice of the action upon the Commission and provide the Commission with a copy of its complaint, and the Commission shall have the right (A) to intervene in the action, (B) upon so intervening, to be heard on all matters arising therein, and (C) to file petitions for appeal.

(4) Any civil action brought under this section in a district court of the United States may be brought in the district wherein the defendant is found or is an inhabitant or transacts business or wherein the telemarking occurred, is occurring, or is about to occur, and process in such cases may be served in any district in which the defendant is an inhabitant or wherever the defendant may be found.

(c) The court, in issuing any final order in any action brought under subsection (b) of this section, may award costs of suit and reasonable fees for attorneys and export witnesses if the plaintiff prevails.

(d) Nothing in this section shall restrict any right which any person may have under any statute or common law to seek enforcement of this Act or any rule, regulation, or order under this Act or to seek any other relief.

VENUE; SERVICE OF PROCESS

SEC. 6. (a) Subsections (a) and (b) of section 13 of the Federal Trade Commission Act (15 U.S.C. 53) are each amended by adding at the end thereof the following: "Whenever it appears to the court that the interests of justice require that any other person, partnership, or corporation should be a party in such suit, the court may cause such person, partnership, or corporation to be summoned without regard to whether they reside or transact business in the district in which the suit is brought, and to that end process may be served in any district.".

(b) Section 13 of the Federal Trade Commission Act (15 U.S.C. 53) is amended—

(1) by redesignating subsection (c) as subsection (d); and

(2) by inserting immediately after subsection (b) the following:

"(c) Any process of the Commission under this section may be served by any person duly authorized by the Commission—

"(1) by delivering a copy of such process to the person to be served, to a member of the partnership to be served, or to the president, secretary, or other executive officer or a director of the corporation to be served;

"(2) by leaving a copy of such process at the residence or the principal office or place of business of such person, partnership, or corporation; or

"(3) by mailing a copy of such process by registered mail or certified mail addressed to such person, partnership, or corporation at his, her, or its residence, principal office, or principal place of business.

The verified return by the person serving such process setting forth the manner of such service shall be proof of the process, and the return post office receipt for such process mailed by registered mail or certified mail as provided in this subsection shall be proof of the service of the process.".

SUBPOENA

SEC. 7. (a) Section 20(a) of the Federal Trade Commission Act (15 U.S.C. 57b–1(a)) is amended—

(1) by redesignating paragraph (7) as paragraph (8); and

(2) by inserting immediately after paragraph (6) the following new paragraph:

"(7) The term 'physical evidence' means any object or device, including any medical device, food product, drug, nutritional product, cosmetic product, or audio or video recording.".

(b) Section 20(c)(1) of the Federal Trade Commission Act (15 U.S.C. 57b-1(c)(1)) is amended—

(1) by inserting "physical evidence or" immediately after "any" the second time it appears;

(2) by inserting "to produce such physical evidence for inspection," immediately before "to produce";

(3) by inserting "physical evidence," immediately after "concerning"; and

(4) by inserting "evidence," immediately before "material, answers,".

(c) Section 20(c)(3) of the Federal Trade Commission Act (15 U.S.C. 57b-1(c)(3)) is amended—

(1) by inserting "physical evidence or" immediately before "documentary material";

(2) in subparagraph (A)—

(A) by inserting "physical evidence or" immediately before "documentary"; and

(B) by inserting "evidence or" immediately after "permit such";

(3) in subparagraph (B), by inserting "evidence or" immediately before "material"; and

(4) in subparagraph (C), by inserting "evidence or" immediately before "material".

(d) Section 20(c)(10) of the Federal Trade Commission Act (15 U.S.C. 57b–1(c)(10)) is amended by inserting "physical evidence or" immediately before "documentary material" each place it appears.

CLEARINGHOUSE

SEC. 8. The Commission shall establish a clearinghouse for inquiries made to Federal agencies concerning telemarketing. The clearinghouse will provide information (other than information which may not be disclosed under section 552(b) of title 5, United States Code, or under regulations prescribed by the Commission to implement section 552(b) of title 5, United States Code) to anyone making inquiries restricting persons engaged in telemarketing or direct such inquiries to the appropriate Federal or State agency.

ADMINISTRATION AND APPLICABILITY OF ACT

SEC. 9. (a) Except as otherwise provided in sections 4 and 5 of this Act, this Act shall be enforced by the Commission under the Federal Trade Commission Act (15 U.S.C. 41 et seq.).

(b) The Commission shall prevent any person from violating a rule, regulation, or order of the Commission under this Act in the same manner, by the same means, and with the same jurisdiction, powers, and duties as though all applicable terms and provisions of the Federal Trade Commission Act (15 U.S.C. 41 et seq.) were incorporated into and made a part of this Act. Any person who violates such a rule, regulation, or order shall be subject to the penalties and entitled to the privileges and immunities provided in the Federal Trade Commission Act in the same manner, by the same means, and with the same jurisdiction, powers, and duties as though all applicable terms and provisions of the Federal Trade Commission Act were incorporated into and made a part of this Act.

(c) Nothing in this Act shall be construed to vest the Commission, the attorney general of any State, or any person with jurisdiction or authority over any person in addition to any jurisdiction or authority granted to the Commission in the Federal Trade Commission Act.

Senator McCain. Mr. Chairman, I would ask unanimous consent that a letter from the Federal Trade Commission to me dated March 16 with their analysis and support—I repeat, support—of my legislation by the FTC, be made part of the record, and I thank you, Mr. Chairman.

Senator Bryan. Thank you very much, Senator McCain. That letter will be made part of the record, and we appreciate very much your leadership in this role.

We have with us this morning one of our colleagues from the other body who has long been identified as an advocate of legislative reform in the area of telemarketing fraud. He is the sponsor of H.R. 1354, Congressman Luken from the First Congressional District of Ohio. Welcome to our Subcommittee. We are delighted to have you here with us this morning, sir.

STATEMENT OF HON. THOMAS A. LUKEN, U.S. REPRESENTATIVE FROM OHIO

Mr. Luken. Thank you, Mr. Chairman.

Senator Bryan and Senator McCain, I am very pleased to be here and to recognize your efforts. Senator McCain in his comments has indicated that we are all on track and heading for a legislative solution, or at least a legislative plan of action that will help in resolving these problems, which we all recognize exist for the American consumer.

So I congratulate you for holding this hearing and hope that we can in some way contribute something towards resolving any differences that may remain, since we do all have that resolve.

I would like to testify on the two Senate bills dealing with telemarketing fraud.

I am happy to say that your bill, Mr. Chairman—S. 2494—has the same essential elements as in our bill in the House, which is H.R. 1354. Both bills direct the Federal Trade Commission to issue within 180 days rules governing marketing. Our bill mandates such rules and your bill, I believe, does not quite go that far, but in any event I think that is very close.

Both bills authorize the State Attorneys General and private citizens to sue in Federal Court those telemarketing firms who either commit fraud or violate the FTC's rules. Both bills make it clear that we seek to supplement what the States are doing and not to preempt them.

There are of course differences between our bills on the precise question of which telemarketing industries are covered, but I would expect that differences of this type could be resolved fairly easily in conference.

I would like again to recognize that you seem to have the spectrum of interests covered, and it is good that Chairman Steiger will be testifying, so that I think you will be able to get to the bottom of it in a hearing such as this today.

I would like to briefly share with you what we have learned in our hearings, very briefly, to show why we must improve the current law enforcement system in the telemarketing area. The current situation, as you know, Mr. Chairman, and your bill recognizes, is that states and private citizens can only sue in state court, and the FTC sues in the Federal court. That dichotomy is unfortunate. Both consumers and legitimate businesses are being hurt by telemarketing scams that are national in scope, and so are difficult to stop by relying on state courts only.

For many people the telephone is becoming a way to reach out and rob someone.

In recent years the FTC has devoted a growing portion of its resources to combating telemarketing fraud in the context of a shrinking total budget of the FTC. Last year the FTC informed our subcommittee that it spent $2.3 million in fiscal year 1988 on telemarketing cases, compared to $411,000 in fiscal year 1983. That would sound pretty good if taken alone and out of context. This is a six-fold increase in the FTC resources devoted to telemarketing.

However, during the same six-year period, the number of work years at the FTC overall shrank by 25 percent, from 1,310 to 986 years. I am afraid what this suggests is that the important work on such matters as mergers and national advertising—we found that in the tobacco area, for example—is being neglected by the FTC because of the shrinking budget.

The FTC has had only limited success in achieving results in the telemarketing area. The FTC told our subcommittee that from 1982 through 1989 the FTC brought 33 Federal court actions against telemarketing scams, and actually recovered about $23 million for consumers. That means the FTC is recovering for consumers less than 1 percent of what the FTC estimates consumers are actually losing.

Moreover, $15 million of what the FTC recovered during that seven-year period, more than half of what is actually recovered, was obtained in a single action in 1983.

The states, as you know, Mr. Chairman, are vigorous in their efforts to stop telemarketing fraud. They are to be congratulated. Attorney General McKay is here, and he is a leader in that area, and he has testified before our subcommittee and has worked very diligently on this area. And I see he is still at it, and I congratulate him for doing that, and I think we are going to achieve success.

Our subcommittee was told that in 1987 and 1989 the attorneys general brought over 150 actions in state courts against fraudulent telemarketing firms, and I understand that some states, such as Nevada, are passing new laws to try to cope with telemarketing fraud.

The same telemarketing firm is frequently sued in Federal court by the FTC and in state court by a state. For example, in 1987 and 1988, the FTC brought 20 telemarketing cases in Federal court. Information given to our subcommittee by the FTC and the states indicates that in at least half of these 20 cases, one or more states sued in state court, the same firm the FTC had sued in Federal court. In nine of these 10 matters, a state sued in state court before the FTC sued in Federal court.

This experience demonstrates very clearly the need for states to have the ability to sue in the Federal court. Even under the capable leadership of the new FTC chairman, Chairman Steiger, the FTC will never be able to handle the job all by itself. That is our belief. And the FTC, even with its regional offices, will rarely be able to move as quickly in telemarketing scams as the states can.

I can well understand why the FTC is a little nervous about sharing its law enforcement role with the states and private citizens. We are all a little jealous of our jurisdiction.

However, the enforcement structure set forth in both your bill, Mr. Chairman, and our bill, of having the national rules promulgated by a Federal agency and being jointly enforced by other Federal agencies, the states and private parties is used by the National Highway Traffic Safety Administration in the area of odometer fraud, for example. It is also used in some Federal environmental laws, such as the Solid Waste Disposal Act, which is under our jurisdiction, and the Noise Control Act. So there is plenty of precedent for going in this direction.

As the Supreme Court made clear this week in the case involving a supermarket merger in California, states and private parties have the right to sue to enforce the Federal antitrust laws, along with the FTC and the Department of Justice—another clear precedent.

Both your bill, Mr. Chairman, and our bill, gives the FTC the right to intervene in any state or private action brought in Federal court. This provision will help ensure the important goal of having the Federal courts enforce the law in a uniform way throughout the whole country.

It has been suggested by the FTC, at page 8 of Chairman Steiger's March 16th, 1990 letter to Senator McCain, that it might be unconstitutional for the states to enforce the FTC's regulations. The sole case cited there by the FTC is Buckley v. Valeo. The Congressional Research Service has told us that this argument is not of great merit. Buckley dealt with the constitutionality of having some members of the Federal Election Commission appointed by Congress, and so dealt with the separation of powers among the Congress, president and judiciary. Buckley did not address the federalism issue of delegating to the states the enforcement of Federal law. The constitutionality of such a key aspect of our Federal system was upheld by the Supreme Court in 1918.

Mr. Chairman, more recently a federal court has upheld the constitutionality of letting states enforce the Federal antitrust laws.

I realize that there remains some controversy, although I think the area of that controversy is narrowing, rather than widening with regard to this important legislation.

I know that direct marketers, for example, say that we cannot trust the attorneys general, or at least they have told us that, to restrict themselves to their business, shall we say. That there is a danger that we will have a whole bunch of runaway attorneys general out there who are being overzealous and carrying out their duties or carrying out the assignment in the newfound jurisdiction in a reckless way.

When this testimony was offered before our subcommittee, we asked these witnesses who expressed that reservation and that fear to give us some example of where the attorneys general have acted in this reckless and heedless way. And thus far, they have not given us any examples of any experience to rely upon as a foundation for that fear.

So we think the attorneys general, on the contrary, have been acting responsibly when they have been given this kind of responsibility, and we think they will in this particular case.

So we look forward to working with you in the remaining months of the 101st Congress, hopefully to a satisfactory solution which will encompass the principles of all of our legislation.

Thank you, Mr. Chairman.

Senator **Bryan**. Thank you very much, Congressman Luken. We look forward to working with you, as well.

I think, as you pointed out during the course of your testimony, there are a number of parallels in the approaches that we have taken, and I, too, am hopeful that we are going to be able to process some legislation.

So we thank you for your leadership and for your support. We will continue to work together, and hopefully we will get something by the end of the session.

Let me defer now to my colleague, Senator McCain, if he has any questions.

Senator **McCain**. No, thank you.

Thank you.

Senator **Bryan**. Thank you very much, Congressman. We appreciate your being here this morning.

Mr. **Luken**. I have been let off easy.

Thank you.

Senator **Bryan**. We will give you a pass today.

Mr. **Luken**. Thank you.

Senator **Bryan**. Thank you very much.

As I noted earlier, we have been joined this morning by the Chairman of the Federal Trade Commission, Janet Steiger, and she joins us now. And we would invite her to the witness table.

Once again, I do not know whether you were in the room when we made a preliminary observation that we recognize you have had an extraordinary hearing schedule, and this subcommittee greatly appreciates your being here this morning. We look forward to hearing your testimony.

STATEMENT OF HON. JANET STEIGER, CHAIRMAN, FEDERAL TRADE COMMISSION, ACCOMPANIED BY BARRY CUTLER, DIRECTOR, BUREAU OF CONSUMER PROTECTION

Ms. **Steiger**. Thank you, that is kind, Senator.

We are committed to assisting in whatever way we can in what we consider to be the very important work that this committee brings forward in the area of telemarketing fraud. And I am delighted to join you this morning to discuss the Commission's views on S. 2494 and S. 1441, introduced respectively by Senators Bryan and McCain.

The bills are aimed at combating telemarketing fraud. It is a matter of serious concern to consumers and the Commission. Estimates have already been mentioned this morning that consumer loss may be over a billion dollars a year to telemarketing scam artists. I personally think that figure could be understated.

The Commission has, consequently, greatly increased its law enforcement efforts in recent years. We have brought 50 telemarketing fraud cases in Federal court. We have obtained permanent injunctions against companies having aggregate sales of over $766 million.

The problem is widespread. It touches on every state and consumers of every age and every class. And the Commission fully supports the objectives of Senate bills 2494 and 1441 to bring greater state resources to bear on this nationwide problem.

We have enjoyed a close working relationship with the states on a host of fraud investigations and cases, and we have established a fraud data bank that provides valuable information exchanges on investigations and cases. And we applaud the states for their efforts in this area, and fully encourage continued cooperation to eradicate telemarketing fraud.

In addressing some of the specific provisions of the bills, we would first like to express our support and appreciation for the increased enforcement tools provided in both bills. Specifically, the broad venue and service of process provisions in the bills will make it easier for us to attack the source of many telemarketing frauds, namely the suppliers of bogus products and others who knowingly aid and abet fraudulent boiler rooms.

Often the parties involved in the telemarketing scam are spread out over many states and jurisdictions, making it difficult to bring all of the defendants before one court. And with the improved venue provisions, we can more easily sue in one court the fraudulent boiler rooms, as well as their out of state suppliers, financiers, or other entities who provide knowing and substantial assistance to the fraud.

In addition, I would like to mention the improved investigative tools given to us in these bills. First, both bills would allow the Commission to require the production of physical evidence pursuant to a civil investigative demand. This will enable us to obtain for purposes of examination or appraisal the actual fraudulent products being telemarketed, such as coins or art.

In addition, the financial data provisions of S.1441 will enable the Commission to discover important financial information about the targets of our investigation, without disclosing to those targets the existence of an investigation.

We believe such a provision will greatly help us preserve whatever assets are available for eventual distribution to defrauded consumers.

As for the rulemaking required by each of the bills, we should point out the Commission is already addressing the question of whether the mail order rule which addresses delayed shipment should be extended to telephone sales generally.

On November 28, 1989, the Commission published a notice of proposed rulemaking to consider whether such an amendment of the rule is desirable. Public hearings on the rulemaking have been held and the record remains open until June 4 for receipt of rebuttal comments by rulemaking participants.

We believe that this rulemaking will provide the most comprehensive basis on which to decide whether the benefits of extending the delayed delivery requirements of the mail order rule to telephone sales would outweigh the costs. This may be a matter best left to normal Commission review and rulemaking processes.

Finally, I would like to address the important issues raised by the State and private enforcement provisions of the bills. Section 4 of S. 2494 would authorize State attorneys general to bring civil actions in Federal district court, one, to enforce compliance with the new telemarketing rule or any orders issued under the rule; and, two, to bring actions on behalf of their residents with respect to a new Federal cause of action for "fraudulent acts or practices."

From the Commission's standpoint, S. 2494 contains laudable improvements over some other bills that have provided for direct State enforcement of broader causes of action under the FTC Act. The bill appears to confine State enforcement to the new telemarketing rule prescribed under the Act and to telemarketing involving fraudulent acts and practices.

This rule, presumably providing for fairly specific prohibitions, should not pose significant problems of inconsistent enforcement of the FTC Act. However, I should note that provisions aimed more directly at hard core fraud may be difficult to define with great specificity, possibly posing problems of inconsistent interpretation.

While I applaud the improvements in S. 2494 over some previous bills, I believe that the State appointments mechanism set forth in S. 1441 would have greater potential for increasing State and Federal cooperation in attacking telemarketing fraud.

The appointments provision of S. 1441, rather than authorizing direct State enforcement of an FTC telemarketing rule, explicitly authorizes the Commission to appoint State attorneys general to assist the Commission in general rule enforcement. I believe such arrangements with the States could achieve much the same objectives as section 4 of S. 2494.

Moreover, this appointments provision could be amended to encompass permanent injunction cases under section 13(b) of the FTC Act against telemarketers engaged in fraudulent practices. It is these section 13(b) fraud cases by which the Commission ordinarily attacks hard core fraud, not rule enforcement.

So expanded, the appointments provision would place the States in a position to participate in nationwide redress cases against hard core fraud under the FTC Act. The Commission and the States could work out arrangements to ensure speedy joint action against fraud while preserving consistent enforcement of the FTC Act.

Section 5 of S. 2494 gives private citizens the right to bring a civil action in Federal district court to, one, enforce compliance with any Commission rule, regulation or order that has been violated by the act of telemarketing and, two, to seek relief for violations of the new Federal cause of action for fraudulent acts or practices.

Other than the requirement that the amount of controversy must be $50,000, the private right of action provisions of section 5 parallel the State enforcement provisions of section 4. As stated above with respect to the State enforcement provisions, we assume that the fraud cause of action has not been made part of FTC doctrine. If correct, this private right of action provision poses no direct threat of inconsistent application of the Act.

Nevertheless, the prospect of private parties enforcing a vague new fraudulent act or practice cause of action may raise concern for legitimate telemarketers. There is a risk that the bill would have the unintended effect of creating a new Federal cause of action applicable to ordinary business transactions rather than the intended target, which is quasi-criminal activity.

This issue has been raised in the considerable controversy over private plaintiffs' use of the RICO statute in litigation over garden variety business disputes.

While I have not touched on each provision of the two bills in my comments here today, I do want to stress the Commission's continued support for the intent of both of these bills. Each contains important enforcement tools that will greatly increase the Commission's efforts in the continuing fight against telemarketing fraud. The bills also present alternatives for increased cooperation between the Commission and the States.

While the precise nature of this Federal-State cooperation can take many forms, it is crucial that the cooperation continue. We have achieved much in the past several years and these bills contain provisions that could increase our success in the future.

Mr. Chairman, that concludes my excerpted remarks from what you know is very lengthy testimony. With your permission, I would submit the full Commission testimony for the record.

Senator BRYAN. That will be done, and the full text of your statement and appendices attached thereto will be made a part of the record.

[The statement follows:]

STATEMENT OF THE FEDERAL TRADE COMMISSION

Mr. Chairman and members of the Subcommittee: I am Janet Steiger, Chairman of the Federal Trade Commission. I appreciate this opportunity to appear before you today on behalf of the Commission to discuss our views on S. 2494 and S. 1441, introduced by Senators Bryan and McCain, respectively.[1]

These bills are aimed at combatting telemarketing fraud, a matter of serious concern to consumers and the Commission. It is estimated that consumers may lose over a billion dollars a year to telemarketing scam artists.[2] Recognizing this threat, the Commission has greatly increased its enforcement efforts in this area. In recent years, the Commission has brought over 50 telemarketing fraud cases in federal court, obtaining injunctions against companies having aggregate sales of over 766 million dollars.

Before addressing the bills, I should first mention two important areas of emphasis in our telemarketing fraud program.

First, we are increasing our efforts to attack the root of fraud, such as suppliers and other aiders-and-abettors. One problem in attacking only boilerrooms is their fly-by-night nature. At times, boilerrooms will pull up roots and destroy documents upon suspecting detection, only to reappear elsewhere under other names. Recognizing this, the Commission, in the investment fraud area especially, already has brought cases not only against boilerrooms, but also against suppliers of rare coins and fake art, promoters of gold mining schemes, and other entities centrally positioned in fraudulent schemes. More can be done, however. In many types of fraud, there are companies that profit from providing knowing assistance to fraudulent boilerrooms in the form of financial assistance and guarantees, references, products for sale, and other critical items and services. If such firms know they may be held responsible for their own participation in the fraud, they undoubtedly will give more care to the decision whether, and on what terms, to deal with fraudulent telemarketers. Our goal is to create a situation where unlawful boilerrooms have difficulty getting started because previously insulated businesses are unwilling to deal with them.

---

[1] Except as noted, the views expressed in this statement represent the views of the Commission. Commissioner Strenio does not agree with all of the discussion concerning the state enforcement provisions and will forward his views in a separate statement. My oral presentation and responses to questions are my own and do not necessarily reflect the views of the Commission or any individual Commissioner.

[2] This figure is based on industry information acquired by FTC staff developing telemarketing fraud cases. This figure is also consistent with estimates of other industry observers and law enforcement agencies. We recognize that by some estimates, the figure may even be higher.

Another area of emphasis for the Commission in enforcing telemarketing fraud is increased cooperation with the states. The Commission fully supports the objectives of S. 1441 and S. 2494 to bring greater state resources to bear on the problem. We have enjoyed a close working relationship with the states on a host of fraud investigations and cases, routinely sharing information, referring cases to one another, and, in some cases, bringing suits in tandem. The Commission has further encouraged federal-state cooperation through the establishment of a fraud data bank. We applaud the states for their efforts in this area.

We should mention one important aspect of state involvement, however. Federal and state resources are limited, and it is important that these resources be concentrated in the most effective manner. In this connection, it is critical that these legislative initiatives not have the unintended effect of drawing resources away from criminal enforcement by the states. Much telemarketing fraud is criminal activity offering huge profits to the perpetrators. Civil law enforcement actions can substantially hinder the activities of scam operators, but it is criminal prosecution that they fear most. Increased criminal enforcement by the states is indispensable to the war on telemarketing fraud.

The Commission already has submitted extensive written comments on S. 1441 to Senator McCain, by way of our letter of March 16, 1990. We have attached these comments on S. 1441 to this statement for inclusion in the hearing record. For clarity's sake and to avoid repetition, the text below will focus principally on S. 2494, comparing its provisions to those of S. 1441 as necessary.

Telemarketing Rule

Section 3 of S. 2494 requires the Commission to promulgate a telemarketing rule and to consider imposing requirements such as refunds for delayed shipment of goods and a cooling-off period. There are similar provisions in S. 1441.[3]

As we stated in our comments on S. 1441, we question whether these provisions are likely to provide significant benefits to consumers who have been victimized by telemarketing scams. First, the Commission already is addressing the broader question of whether the protections of the Mail Order Rule should be extended to telephone sales. On November 28, 1989, the Commission published a Notice of Proposed Rulemaking to consider whether such an amendment of the Rule is desirable. 54 Fed. Reg. 49,060 et seq. (November 28, 1989). Public hearings on the rulemaking have been held and the record remains open until June 4 for receipt of rebuttal comments by rulemaking participants. We believe that this rulemaking will provide the most comprehensive basis on which to decide whether the benefits of extending the delayed-delivery requirements of the Mail Order Rule to telephone sales would outweigh the costs. This may be a matter best left to normal Commission review and rulemaking processes.

More fundamentally, such extensions of the Mail Order Rule relate more to problems encountered in routine business transactions than to the target of both bills -- hard-core fraud. The typical telemarketing fraud does not involve delayed shipment. Rather, the heart of the fraud is deception regarding the nature, value, quality, or cost of the products or services sold. It is this deception that has cost consumers billions of dollars over the years. Similarly, the cooling-off provision contemplated in § 4(a)(2) of S. 2494 would not affect the vast majority of fraudulent telemarketing transactions, because the consumer typically is unaware that he or she has been defrauded until long after the initial transaction.

---

[3] S. 1441 requires the Commission to amend its Mail Order Rule, 16 C.F.R. 435 (1987), to cover telephone sales and to consider a cooling-off requirement.

S. 2494, in contrast to S. 1441, further requires the Commission to consider restrictions on the time of day that telemarketers can make unsolicited calls to consumers, as well as prohibitions on the use of computer equipment that does not permit consumers to immediately terminate calls. We recognize that harassing, abusive, and late night telephone calls are legitimate concerns. However, in our experience it has been the substance of the sales pitch and the resulting sale of overvalued goods and services that has caused significant consumer injury in telemarketing fraud cases. Scarce law enforcement resources should remain targeted at the core of the fraud.

The above notwithstanding, we appreciate the explicit authorization to conduct whatever telemarketing rule as may be required pursuant to the notice-and-comment provisions of 5 U.S.C. § 553. It would be difficult, if not impossible, to conduct the contemplated rulemaking within the 180-day deadline under the more complex procedures of The Magnuson-Moss Warranty - Federal Trade Commission Improvement Act, 15 U.S.C. § 2301. We urge one addition to S. 2494, however -- explicit authorization for the Commission to seek civil penalties for violation of this section 553 rule. Currently, the Commission only has the authority to seek civil penalties for violations of rules regulating unfair or deceptive acts or practices that are promulgated under the authority of the FTC Act. The foregoing amendment would make clear that the Commission could seek civil penalties for violations of the rule contemplated in S. 2494, even though the bill, rather than the FTC Act, would have been the impetus for number of the rule's provisions.[4]

The State Enforcement Provision in S. 2494

Section 4 of S. 2494 would permit state attorneys general to bring a civil action in federal district court (1) to enforce compliance with the new Commission telemarketing rule and orders obtained thereunder,[5] and (2) to bring actions on behalf of their residents with respect to a new federal cause of action for "fraudulent act[s] or practice[s]."

---

[4] An example is the language in the "Petroleum Marketing Practices Act," 15 U.S.C. § 2801 et seq. The Act required, inter alia, that the Commission promulgate the Octane Labeling Rule under the notice-and-comment procedures of 5 U.S.C. § 553. The Act went on to say that "[f]or purposes of the Federal Trade Commission Act (including any remedy or penalty applicable to any violation thereof) such a violation shall be treated as a violation of a rule under such Act respecting unfair or deceptive acts or practices . . . ."

[5] Specifically, § 4(a)(1) provides for state actions with respect to telemarketing "which is a fraudulent act or practice or which violates any rule, regulation, or order of the Commission under this Act." "This Act" presumably refers to S. 2494, rather than the FTC Act.

From the Commission's standpoint, S. 2494 contains laudable improvements over other bills that have provided for direct state enforcement of broader causes of action incorporated in the FTC Act. In previous testimony on such bills, we had expressed our concern that direct state enforcement of broad causes of action incorporated in the FTC Act could result in inconsistent application of the Act nationwide. As the number of agencies enforcing the Act increases, so too does the potential for inconsistent enforcement and court decisions. In choosing cases and strategies, the Commission is in the best position to take into account the effect of precedent on issues affecting its other programs.

S. 2494, however, appears to provide for state enforcement only with respect to the proposed telemarketing rule and orders obtained thereunder. Assuming that the practices covered by the rule can be defined with specificity,[6] there should not be a significant problem of inconsistent enforcement of the FTC Act. Moreover, it appears that the broader "fraudulent act or practice" cause of action in S. 2494 is not intended to be incorporated in FTC Act doctrine.

We also note that S. 2494 only authorizes states to bring damages suits and other actions "on behalf of their residents."

---

[6] As noted above, however, the specific prohibitions now contemplated for inclusion in the rule (e.g., cooling-off periods), are unlikely to significantly affect hard-core fraud. It may be that further rule provisions that more directly attack the problem would be difficult to define with specificity, raising some problems of inconsistent enforcement.

This parens patriae scheme should pose less chance of being challenged in court as unconstitutional under the Appointments Clause than statutes authorizing states to enforce broad federal rights in the same manner as the Commission. The Department of Justice, commenting on other bills, had opined that such provisions are unconstitutional, involving the exercise of "significant authority pursuant to the laws of the United States" by persons not selected in accordance with the Appointments Clause (quoting Buckley v. Valeo, 424 U.S. 1 (1975)).[7]

In any event, further definition of "fraudulent act or practice" may improve the bill. That term, not defined in S. 2494, also has not been defined in consistent fashion in federal and state criminal and civil statutes and common law.[8]

The State Appointment Provision in S. 1441

While we applaud the improvements in S. 2494 over some previous bills, we believe that the state appointments scheme set forth in S. 1441, expanded as suggested below, would have greater potential for increasing state-federal cooperation in attacking telemarketing fraud.

---

[7] Letter from Thomas M. Boyd, Acting Assistant Attorney General, Office of Legal Policy, U.S. Department of Justice, to the Hon. John McCain, United States Senate, September 27, 1988.

[8] We also recommend that § 4(a)(3) of S. 2494 be amended to provide reasonable advance notice to the Commission of the filing of federal court actions by the states, to facilitate exercise of the intervention rights set forth therein.

Section 4(e) of S. 1441, rather than authorizing direct state enforcement of its proposed telemarketing rule, explicitly authorizes the Commission to appoint state attorneys general to assist the Commission in general rule enforcement. We believe such arrangements with the states could achieve much the same objectives as section 4 of S. 2494. In the attached comments on S. 1441, we have suggested an expansion of the appointments scheme to include permanent injunction cases brought under section 13(b) of the FTC Act against fraudulent telemarketers. The Commission ordinarily attacks hard-core fraud by bringing such section 13(b) cases, rather than by rule enforcement. We also urged that the Commission be authorized to appoint not only state attorneys general, but also other officials granted civil or criminal law enforcement authority under state law.

There are several advantages to this appointments scheme. The states would be in a position to participate in nationwide redress cases against hard-core fraud under the FTC Act. The Commission and the states could work out arrangements to ensure speedy joint action against fraud, while preserving consistent enforcement of the Act. We should also note that the appointments system does not pose the constitutional risks of alternatives that provide for full unilateral state enforcement of the FTC Act and its nationwide remedies.[9]

---

[9] The suits "on behalf of their residents" by states to enforce the telemarketing rule, as contemplated in S. 2494, also pose less risk of constitutional challenge compared to these broader state enforcement schemes.

Private Right of Action

Section 5 of S. 2494 gives private citizens the right to bring a civil action in federal district court (1) to enforce compliance with the new Commission telemarketing rule and orders obtained thereunder, and (2) to seek relief for violations of the new federal cause of action for "fraudulent act[s] or practice[s]."[10] Other than the requirement that the amount in controversy exceed $50,000, the private right of action provisions of section 5 parallel the state enforcement provisions of section 4.

As stated above with respect to the state enforcement provisions, we assume that the fraud cause of action is not intended as an addition to FTC doctrine. Nevertheless, the prospect of private parties enforcing a vague new "fraudulent act or practice" cause of action may raise concern for legitimate telemarketers. In our previous testimony on similar provisions, the Commission observed that there was risk that the bills would have the effect of creating a new federal cause of action applicable to ordinary business transactions rather than to the intended target, i.e. quasi-criminal activity. This issue has surfaced in the considerable controversy over private plaintiffs' use of the RICO statute in litigation over garden-variety business disputes.[11]

---

[10] We assume that the reference in section 5 of S. 2494 to private parties bringing actions "on behalf of their residents" was unintended.

One problem is the inherent difficulty of defining "telemarketer" and "telemarketing" with adequate specificity. While the bill makes a laudable effort in that regard, the intended scope of activity remains unclear. As defined in the bill, the term "telemarketing" means "a plan, program or campaign conducted to induce purchases of goods or services by significant use of one or more telephones through interstate voice telephone calls; the term does not include other use of a telephone in connection with business or personal transactions." "Significant" is not defined, meaning the court would have to decide whether one telephone call or one hundred satisfies the bill's definition.

Moreover, this problem is compounded by the vagueness of the term "fraudulent act or practice" itself. Without further definition, the term arguably applies in any instance where a person believes he or she was intentionally misled in an ordinary business transaction conducted over the telephone.

Venue and Compulsory Process

As discussed in the Commission's letter of March 16, 1990, to Senator McCain, we have experienced problems with the venue provisions of section 13 of the FTC Act, our most common tool in attacking consumer fraud. There have been cases where staff, confronted with venue problems, could not bring meritorious claims against participants in fraud who did not reside or transact business in the forum state.

---

[11] Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. § 1961 (1982 & Supp. IV 1986).

This problem will grow in importance as the Commission increases its enforcement efforts against suppliers of fraudulent instrumentalities and other aiders-and-abettors of boilerroom fraud. Frequently, the more complex schemes involve a network of firms and individuals spread over many states. Getting at the root of such frauds often will involve suing the principal aider-and-abettor in its home jurisdiction, and trying to join as defendants as many of the participating boilerrooms as possible, wherever located.

Section 6 of S. 2494, like section 4 of S. 1441, would remedy these venue problems by making it clear that the Commission may sue all such defendants in one district when a federal court finds that the ends of justice so require. This would be a welcome amendment to our statute. As in the case of S. 1441, we would recommend the addition of language to allow the court to serve its process on the defendant "wherever it may be found."[12] Without such a provision, service of a summons outside the state in which the court sits depends upon the vagaries of state long-arm statute requirements, which in particular instances may not be broad enough to reach out-of-state defendants. Congress has provided for such extraterritorial service of process in similar contexts. See, e.g., 15 U.S.C. § 22 (Clayton Act); 18 U.S.C. § 1965 (RICO); 15 U.S.C. § 77v(a) (SEC).

---

[12] Our specific proposed amendment can be found in footnote 2 of the letter to Senator McCain.

Both bills would further amend the FTC Act to address, for the first time, the manner in which the Commission may serve process in section 13 actions (section 6(b) of S. 2494 and section 4(a)(2) of S. 1441). Currently, the Commission serves process pursuant to the provisions of Rule 4 of the Federal Rules of Civil Procedure. Essentially, Rule 4 gives the Commission the service-of-process options set out in the Rule itself, or those provided by relevant state law. We have no objection to the substitute service-of-process provisions in these bills, but note that the current scheme has proved satisfactory. As with S. 1441, we would recommend one change to section 4(a)(2), however. The phrase "any process of the Commission" should be changed to "process of the court," to reflect the fact that section 13(b) cases are brought in federal court.

Finally, we strongly support section 7 of S. 2494, which, like S. 1441, would amend the FTC Act to enable the Commission to require the production of physical evidence pursuant to civil investigative demands. Currently, section 20 of the FTC Act only permits the Commission to require the production of documents or testimony. The above provision in the bill would enhance our ability to investigate telemarketing scams.

Clearinghouse

S. 2494, unlike S. 1441, would require the Commission to provide information to any person inquiring about telemarketers through a clearinghouse to be established by the Commission. We fully support the intent of this provision to enable consumers to obtain information on potential scams before they are defrauded. We also appreciate the bill's recognition of the Commission's need to protect the confidentiality and integrity of our investigations. Given this necessary exemption from disclosure provided in the bill, however, we question whether, in the normal course, we could provide consumers with meaningful information about many companies with which they are dealing. For example, we can not reveal whether a particular company is under investigation. Nevertheless, the clearinghouse could be a source of centralized information regarding the existence of ongoing litigation and the results of completed cases.

Recommended Additions to S. 2494

As in our comments on S. 1441, we recommend that the Subcommittee consider a number of additional provisions that would assist the Commission in its fight against consumer fraud.[13]

---

[13] We note that the Commission also welcomed the requirements in S. 1441 that the Commission conduct studies in the life care nursing home industry and long-term health care insurance industry.

Criminal Contempt Authority

First, we recommend that the bills amend the FTC Act to clarify the Commission's criminal contempt authority with respect to orders it obtains in section 13(b) actions. Specifically, we recommend that section 16 of the FTC Act be amended to explicitly authorize the Commission, after consultation with the Justice Department, to bring criminal contempt actions for violations of orders obtained in such cases. This would be the same consultation procedure by which the Commission now brings civil penalty and other federal court actions as to which it does not now have exclusive litigating authority. As in civil penalty actions, the Justice Department would retain the right of first refusal to bring such actions, to be exercised within forty-five days of notification by the Commission.[14]

The proposed amendment would be an important complement to our enforcement powers under section 13(b) of the FTC Act. As stated before, scam operators are adept at resurfacing with new frauds under new names, and fear criminal prosecution more than civil suits. Staff has encountered instances where scam operators have hidden assets or re-opened new fraudulent businesses in violation of existing court orders. With the above authority, the Commission would be in a position to act quickly against violators of orders, while the Justice Department would retain the option to take action itself.

---

[14] Our specific proposed amendment can be found in footnote 14 of the letter to Senator McCain.

Civil Penalty Authority

Second, we recommend that section 5(m)(1)(B) of the FTC Act be amended to extend the Commission's existing civil penalty authority. Currently, that section authorizes the Commission to bring civil penalty actions in federal court against persons who have actual knowledge that their conduct violates the FTC Act. A pre-condition to such suits is a prior Commission determination in a cease and desist order proceeding that the specific practice is unlawful. Such a Commission order, or synopsis thereof, can be sent to others in the industry who are engaged in the same practice, putting them on notice that they may be charged with civil penalties if they continue this practice.

The Commission cannot exercise this civil penalty authority if a federal court, rather than the Commission, has made the determination that a specific practice violates the FTC Act. We recommend that section 5(m)(1)(B) be amended to permit civil penalty suits where federal courts, as well as the Commission, have made such determinations.[15] This added civil penalty authority would be an important supplement to the existing injunctive and redress remedies in section 13(b) cases. Besides its general deterrent effect, civil penalty authority would provide the Commission with a monetary remedy where redress to consumers or other equitable remedies are impractical.

---

[15] Our specific proposed amendment can be found in footnote 16 of the letter to Senator McCain.

Right to Financial Privacy Act

The Commission ordinarily tries to locate potential defendants' assets before suit is filed. The Commission then requests that the court grant ex parte asset freeze orders that immediately can be served on all relevant financial institutions before the defendants can hide their assets. Obviously, this pre-complaint search for assets must be conducted without alerting the target individuals. The Right to Financial Privacy Act,[16] however, makes this difficult with respect to the assets held by financial institutions for individuals and certain small partnerships. Currently, the Act requires that such customers of financial institutions be notified of federal agency inquiries, with certain exceptions. These exceptions are not specifically tailored to address situations where investigative targets are likely to dissipate assets obtained through fraud.

Section 4(d) of S. 1441 would remedy this problem by adding a new exemption applicable to the routine fraud case. Specifically, federal agencies could delay notice where a federal district court finds, inter alia, that there is reason to believe that notice will result in "dissipation, removal, or destruction of assets that are subject to forfeiture, seizure, redress, or restitution under any law of the United States by reason of having been obtained in violation of law."

We welcome this provision, and recommend its addition to S. 2494. We suggest only one modification to make the process less cumbersome. If the language of section 4(d) of S. 1441 were to be adopted without change, the Right to Financial Privacy Act, arguably, still would require the Commission to file an ex parte, sealed complaint in the home district of every financial institution from which it seeks information.[17] Often, individuals and small partnerships running consumer frauds maintain numerous financial accounts spread over the country. In such circumstances, the search for individual and partnership assets would remain a difficult task. One solution would be to further amend the Right to Financial Privacy Act to permit the Commission and other federal agencies to file applications with "any district court of the United States within the jurisdiction of which such inquiry is carried on." This is the language in section 9 of the FTC Act that describes the courts to which the Commission may apply to enforce subpoenas.

---

[16] 12 U.S.C. § 3401 et seq.

This approach would retain judicial protection of the privacy rights of financial institution customers, while greatly reducing the Commission's time and travel burden. Headquarters staff often could obtain judicial approval in the U.S. District

---

[17] Under 12 U.S.C. § 3409(a), the Government must obtain "an order of an appropriate court" granting the requested delay of notice to the customer and prohibiting the bank from disclosing the government inquiry to the customer. (emphasis supplied) Although "appropriate court" is not defined in the statute, this term could be read as requiring the Government to file the application in the federal judicial district within which the financial institution is located.

Court for the District of Columbia, and Commission regional staff often could obtain court approvals in their home cities.[18]

Thank you once again for the opportunity to provide our views on S. 2494, introduced by Senator Bryan, and S. 1441, introduced by Senator McCain. We would greatly appreciate the opportunity to comment further on any significant revisions, and stand ready to assist you in your further consideration of the bill.

---

[18] Section 4(c) of S. 1441 would have the beneficial effect of granting the Commission access to mail covers, which, under current postal regulations are only made available to agencies in connection with criminal investigations. The language of section 4(c) is an improvement over that of the predecessor bill, S. 2326, in making clear that the Commission would have the same power to obtain mail covers as "law enforcement agencies investigating the commission or attempted commission of a crime." The corresponding reference in S. 2326 was "other law enforcement agencies," which arguably would have included some civil law enforcement agencies that do not have access to mail covers and, unlike the Commission, do not even investigate criminal fraud-type activities.

Senator **Bryan**. We thank you for the testimony.

Let me raise a couple of questions and then I will defer to my colleague, Senator McCain, who I know has questions as well.

Both he and I propose rulemaking to consider what I would consider the harassment aspect. There is a cooling-off period that we have suggested ought to be appropriate for rulemaking, limitation on the hours of day that calls may be made, provisions that would require, after you conduct the rulemaking, if in your judgment it is necessary, to require shipment to occur within certain periods of time, and several other aspects.

As I read your written testimony, you seem to express with respect to S. 1441 as well as 2494 that you do not really see a problem area here. Am I reading that testimony correctly and, if so, I am surprised. Let me just tell you where I am coming from.

People who are solicited in their home or place of business by telephone are psychologically disadvantaged in the sense that they are not in the marketplace actively looking for an appliance or an item, and so therefore make decisions which may be spontaneous and not well considered.

You will recall that over the years most States have provisions for door-to-door sales solicitations, not by phone directly, that provide for a three-day cooling-off period for much the same reason. If I understand your testimony correctly—and I want to give you the opportunity to expand upon that—you seem to think that this is not much of a problem and maybe ought not be the subject of rulemaking by the Commission.

Let me throw that one to you, if I may.

Ms. **Steiger**. I think the thrust of my testimony is not that these could not be matters of import and should be given consideration, but that we are not sure they hit the root cause of the problem.

Frequently in the scams that we have uncovered the calls are not harassing. They are indeed very smooth, extremely friendly, and they are not repetitive in the sense of being intrusive. In addition, the problem is often not that there is any delay in getting you the materials that you have become involved with in one of these scams. Quite the reverse, they may come very promptly indeed.

It is simply they are not of the value or the quality that you had been led to believe they would be. So we are not sure that the proposed solution gets at the root of what we are talking about here, although we see no problem. We do not think that it would interfere with our enforcement. It just may not be the area of emphasis, if we are going to cure telemarketing fraud.

Senator **Bryan**. Let us assume for the sake of argument that with respect to the tonal quality of the invitation to buy that indeed these callers are models of deportment and that none of us could find fault with either the language or the tone used. Let me press you a little bit more specifically on the philosophy of a cooling-off period.

That is to say, assuming all of the above, as you have related to us, should the customer have available to him or to her the right to reconsider that decision, having been made in the sanctity of his or her home or perhaps place of business, where he or she has not invited the call, has not been in the marketplace as such, makes a snap judgment, should not he or she have the right to say, look, no fraud, no misrepresentation; the last thing I need is another vacuum cleaner and to simply be able to cancel it within a timely period.

If I can get you to respond to the philosophy that that rule would suggest.

Ms. STEIGER. Certainly. I can see no harm in that provision and in fact it has been an important provision of the mail order rule, I personally think a successful one.

Again, I would only add that in many of the cases that we have seen it is well beyond the time period of any cooling-off provision that the customer realizes the depth of the fraud that has been perpetrated on him.

I see certainly no harm in it, and perhaps some good. It is just that, there again, it will not cure the whole problem.

Senator BRYAN. And I do not suggest that that is the curative measure that takes care of all of the litany of horrors that Attorney General McKay I am sure is going to share with us in just a few moments.

Let me move next to an area that is troublesome to me as well, and that is the question should we define what we mean by this Federal cause of action for fraud. We have not done so in S. 2494. You have raised a question in your testimony, both oral and written, as to whether or not we might be creating something that is not sufficiently defined.

First, do you think we ought to define it legislatively and, if you do, would you have your able staff submit to us a proposed definition that you think would address any concerns that you might have?

Ms. STEIGER. We would be delighted to work with the Committee staff in this area. I would only note that what constitutes conduct that is fraudulent in an industry that encompasses the provision of services ranging from bargain vacations to oil leases to gold mines and so on and so on involves very difficult and complex issues of deception law.

I do think the number of issues increases the potential for inconsistent application, even as you are trying to define it. But we are more than willing to provide whatever assistance we can.

Senator BRYAN. We would appreciate that, because if there is a concern, and some of the testimony, as you know, later in the hearing expresses that concern, the definition of it is something we would be delighted to work with.

Let me focus now, if I may, on the relationship of the Commission with the attorneys general. Without reciting the sins and misdeeds of the past, as some of us view it, one of the things that impressed me early on when you and I visited privately in my office and later at your confirmation hearing is that you have indicated that you want to renew a positive relationship with the attorneys general.

It is my sense that that is occurring. Would you comment on that? Then I want to ask you about the deputization concept which Senator McCain has in his bill and the more direct enforcement authority that our bill would confer upon States attorneys general.

Ms. STEIGER. I have been very pleased with the response of the states' Attorneys General. I think they have been most forthcoming in offering to work with us to increase our cooperation and communication in times of very scarce assets for all of us.

I think we are aware that wherever we can act in concert or wherever we can act with the best use of our respective assets, it is to the good of the consumer. I think we are making progress, although I will leave that to the Attorney General to comment on.

Beyond that, a recent case illustrates the kind of approach that is improving, I think, our enforcement abilities. We have been joined by several enforcement agencies in the Texas area in a large case against allegedly fraudulent water purifier providers. We were assisted by the state's Attorney General's office, by the Postal Service and just about every other law enforcement agency on the block. This kind of strike force effort has been very successful. You mentioned your state. I am told that when this task force started in 1987, there were some 200 telemarketers who were the subject of many, many consumer complaints, and the number has now been reduced to ten. So, an active multi-pronged enforcement does appear to work.

Senator BRYAN. It has been very helpful.

Ms. STEIGER. Now, they probably moved somewhere else, but at least they are not in your state to the extent that they were. We have had similar success with a multi-agency boiler room task force in California, and I think more of them could be developed on an ad hoc basis as the need arises. But those are some of our initiatives and, yes, I have been delighted with the response of the states' Attorneys General.

Senator BRYAN. Let me ask you to comment. Again, I understand your preference for the deputized approach, and with the greatest respect to my friend and colleague, Senator McCain, who has worked on this legislation for a good many months, the one thing that always impressed me, and once upon a time I had Attorney General McKay's job, long before we knew anything about telemarketing, Attorney General McKay, is that time is of the essence. I have been impressed by the argument he has made and others have made that these are moving targets, if you will. We are talking now about the fraudulent telemarketers, acknowledging that there are many, many legitimate telemarketing businesses.

So the focus of what Senator McCain and I and Congressman Luken and others are interested in should not be interpreted as besmirching the legitimate telemarketer. We are talking about the scam artist, the person that is the object of all of our inquiry and concern. But they are a moving target. This is almost a migratory enterprise in which you can move literally from one side of town to another side of town, from one community to another community.

Not all cities and counties in my own state, and I suspect it is true elsewhere, have the same rules and requirements even to establish a business. Some counties yet today in this country do not require a business license, and you can simply move in. When you look at the interstate aspects of the thing, it makes it all the more difficult, and hence the cause of action is provided for the Attorney General and the venue provisions which you made note of.

Does the deputizing concept recognize the need to act and to act swiftly? Pretty clearly the Attorney General in any given state, because of the resources that he has or she has available to him or to her in that state and the fact that the localized issues are probably going to first come to their attention before it works its way up through the Federal process, gives the Attorney General the unique opportunity to strike, to strike hard, and to move quickly.

I imply no criticism in the approach that we structure, Ms. Steiger, of you or the commission in any way. Would you respond to that concern for me?

Ms. STEIGER. Surely. Let me make a couple of points. First, I do not want ever to leave the impression that we do not encourage the vigorous and rapid enforcement of state laws. Most states have laws against fraud and deception, and we applaud their moving as fast as they can move. We are discussing the area of enforcement of a Federal law. We would like to see the deputization, by the way, extend to the ability to bring action under 13(b) because we think this would give the states the broader redress powers, an effectiveness that our statute does offer them.

As to the question of time, we can move rapidly. Whether we move rapidly enough is always a question, but I think it has to be understood that in these cases when you are going into Federal court and you are asking for a cease and desist order and the freezing of assets, you have to present a rather complicated case, and it does take time. It takes time to develop, given the extreme intricacy of these schemes, the evidence that you can present to win your case, the tracing of the networks that these scams often exist under is complicated. It does take some time.

As a practical matter, if brought in at an early date, I do not think the fact that there is some time in which to get an Attorney General's staff on board would be a problem. The development of these cases does take some amount of time. In any event, we hope that there would be a protocol established for an early entry of the Attorneys General or of their state enforcement agencies, and I add that because we would like to see the appointment authority extended to others who have enforcement efforts underway and who can be useful as well.

So, I think time is less of a problem given the fact that a case does take development in any event, no matter who is doing it.

Senator BRYAN. I certainly appreciate your comment. I know that with your cooperative attitude, I think you would work closely and are working closely with the Attorneys General. As you know, that is a philosophy that has not always been in evidence and, as we draft these pieces of legislation, we need to draft them not only for the personality that is incumbent to the position when it is enacted, but to recognize that there may be circumstances where that relationship that you have cultivated may not exist.

Let me defer now to my friend and colleague, Senator McCain.

Senator MCCAIN. Thank you very much, Mr. Chairman.

Ms. Steiger, in terms of improving relations with the states' Attorneys General I think a case could be made that the major reason for that improvement is your skills and your cooperative effort toward them, and I think that should be recognized. I think it shows that cooperative efforts can succeed, and I think we should at least think hard about changing the law to allow states and private parties to sue without Federal supervision under Federal law in Federal courts. Do you agree with that?

Ms. **Steiger**. I think we have expressed a preference for the appointments mechanism for the reasons that the testimony outlines.

Senator **McCain**. Do other agencies have authorities to appoint state officials for Federal court proceedings?

Ms. **Steiger**. Yes, indeed. The Justice Department and the U.S. Attorneys have such authority, and they have used it successfully to gain assistance from other law enforcement entities at both the Federal and other levels, yes.

Senator **McCain**. So that has worked well in the opinion of the Justice Department?

Ms. **Steiger**. I would defer to Justice's characterization of it, but in my experience they certainly seem to have used it well and smoothly. The clearance process and the like does take some time, but it can be done in advance of any appointments, and it has been used rather frequently.

Senator **McCain**. I want to thank you for your in-depth analysis of the legislation that you provided, and I appreciate very much the overall support expressed in that letter. How many states in the past have asked the FTC to initiate litigation concerning telemarketing fraud?

Ms. **Steiger**. I do not have a number. Can we supply it for the record?

Senator **McCain**. Any? Few? None?

Mr. **Cutler**. We have had some, and we would supply it for the record. I would say recently one of the trends that we have seen is states being willing to work cooperatively and at the same time bringing joint actions with the FTC. I think part of our thought behind the appointment process is that we have been encouraged in the FTC's ability to work with states on a strike force-type basis.

[The following information was subsequently received for the record:]

Senator McCain asked how many states in the past have asked the Commission to initiate litigation concerning telemarketing fraud. It is difficult to answer this question, because there have been no formal procedures for such requests. Indeed, the Commission's entire relationship with the states in the telemarketing area has been characterized by a high degree of "get-the-job-done" informality. Thus, a state official who is starting to look at a telemarketing company may contact our staff to determine whether we are pursuing an investigation of the company. At that point, some discussion is likely to occur concerning the status of the respective investigations, the resources available to pursue them in light of other office priorities, the local or national nature of the company's practices, and so on. Based on these discussions, the state official may suggest that action by the Commission would be the preferable course, freeing the state to pursue other priority investigations. Alternatively, our staff may encourage the state to pursue the matter, given available re sources and low enforcement demands. These discussions, as I have indicated, are very informal—often occurring at the staff member to staff member level—and have been very productive from the Commission's point of view.

Senator **Bryan**. If the Senator would yield, that is Barry Cutler, who is with the office who is responding in part. We welcome, as I am sure Senator McCain does, any response you might care to give.

Ms. **Steiger**. I am remiss in that. Barry is a very able and experienced litigator and head of our Bureau of Consumer Protection, who should have been introduced much earlier. My apologies.

I would note, Senator, that some 26 states have joined in our telemarketing fraud bank, and we do maintain that network with the states in the exchange of information.

Senator **McCain**. What is wrong with the other 24?

Ms. **Steiger**. That is a question that the states' Attorneys General and the commission are discussing. In the past there have been technical problems with having to double enter. In other words, you enter your material in your own system, and then you had to double it. We think we have cured it. We think we have a system now that will allow the states to dump, so to speak, their data and let us reconcile the software. We have provided some further instructions to the states, and I expect more of them to join once it becomes less of a technical problem.

Senator **McCain**. As I said in my opening statement, estimates are that health fraud alone costs Americans about $27 billion a year, and the Food and Drug Administration estimates that 38 million Americans have used a fraudulent health product within the past year, and one out of ten of those people was harmed by side effects. Do you agree with those numbers, basically?

Ms. **Steiger**. I would certainly not disagree, and they may well be conservative. The FTC's experience for many years, we have brought over 80 cases, I believe, in this area. Our experience has been that health care frauds are remarkably resilient. You might cure one, and there will be a new one, and they are of potential, very serious damage to the public because they are in an area where the public cannot for themselves determine the efficacy or safety of the product, and we remain very concerned with that area.

Senator **McCain**. Do you have any idea what percentage of this astounding amount of health fraud is perpetrated through telemarketing and how much occurs through other tactics of general consumer fraud?

Ms. **Steiger**. I do not. Telemarketing fraud runs a gamut that is so awesome that I believe Senator Bryan said only the limits of the mind of man will define it for you. It goes from health frauds to gold in the ground to investment scams, from art to diamonds to precious metals and minerals. There is no end to it. I have not quantified what proportion of our cases have been health care, but it has been one of a range. It seems endless.

Senator **McCain**. In your judgment how important is it that legislation we are considering direct the commission to promulgate rules regarding health care fraud?

Ms. **Steiger**. I have not studied that particular issue. I think that a general authority is probably sufficient to pursue this and almost any other kind of fraud that anyone can think of. I hedge that because someone will come up with a fraud that we may not be able to cover tomorrow. If I say we can cover them all, I think our general authority is probably adequate.

Senator **McCain**. Do you believe that there is a need for the FTC to conduct a study of unfair, deceptive acts or practices in the life care home industry and a study concerning long-term health care insurance?

Ms. **Steiger**. We would welcome that opportunity. As we mentioned in our letter to you, sir, we are barred, of course, from even the study of the business of insurance without specific requests from the appropriate congressional committees. We did provide—the Bureau of Consumer Protection did provide a study at the request of the Congress on Medigap insurance, and one of their conclusions was that the whole life care industry could be a very fruitful one for evaluation. The only caveat we would make on it is that this is a relatively new insurance form out there, and whether there have been enough data generated for us to do a study within a relatively short period of time, we are not sure. But we would welcome the opportunity. We have some expertise in this area, as you know.

Senator McCAIN. I note with some interest in the letter you wrote me that you urged that the Commission authorize not only State Attorneys General but also other officials granted civil or criminal law enforcement authority under State law.

Why do you want to do that?

Ms. STEIGER. The range of fraud may extend to securities, it may extend to something that a district attorney could be very, very helpful in. We just would not want to cut it off to simply one type of law enforcement agent. We think there are others out there with specific expertise. We have worked with everyone from land management agencies to securities and comptroller's offices in the states. You just never can tell what kind of expert help you are going to need, frankly.

Senator McCAIN. Thank you for doing a very outstanding job, thank you for a very illuminating statement, and thank you for all your assistance and cooperation on an issue that has some incredible human elements to it. There are unfolding tragedies in my state as we speak of people who are being deprived of their life savings and their health and well being and are being harmed by these unscrupulous individuals who are preying on them. I thank you for all your work in this area.

Thank you, Mr. Chairman.

Senator BRYAN. Thank you very much, Senator McCain.

I, too, would like to add a personal note of thanks. We appreciate your being here today, as I have noted before, and we look forward to working with you. It is very clear that you recognize that there is not only a role but a need for the State Attorneys General to work with the Commission independently and in concert to address this problem of telemarketing fraud. We will wrestle with some of the issues that have been raised by your testimony and try to process some legislation.

Thank you so very much.

Ms. STEIGER. I wish you well and commend your efforts. Thank you, sir.

Senator BRYAN. Thank you very much.

We will next hear from Attorney General Brian McKay from the State of Nevada speaking on his own behalf and on behalf of the National Association of Attorneys General, who will give us a perspective of the man in the trenches.

Good morning.

STATEMENT OF BRIAN McKAY, ATTORNEY GENERAL, STATE OF NEVADA, ON BEHALF OF THE NATIONAL ASSOCIATION OF ATTORNEYS GENERAL

Mr. McKAY. Good morning, and thank you very much, Mr. Chairman and Senator McCain.

Let me just make a preliminary statement in response to Chairman Steiger's deferral to me about the relationship between the FTC and the states. I would like to say that the difference between the prior leadership of the FTC and that of Chairman Steiger is like the difference between night and day. We have an excellent relationship. It continues to improve, and it is mostly because of the leadership and initiative that she has taken. So let me answer that on her behalf, if I may.

Telemarketing fraud is one of the most serious consumer problems present today. We have heard already that fraudulent telemarketers bilk unsuspecting consumers out of billions of dollars annually, and these unscrupulous operators frequently prey upon senior citizens and the uneducated. They sell products ranging from pens to vitamins to gold bouillon, and their sales techniques vary from promises of prizes to lies concerning the profitability of investments. Regardless of the product or sales technique, the one constant is fraud.

All boilerrooms use high pressure sales techniques. The telemarketer creates a sense of urgency in the consumer through false time limitations such as a very short period to claim a prize or a temporary window of opportunity on an investment. Since the transaction takes place by telephone, the consumer must rely solely on the representations of the telemarketer. The amounts involved in these transactions can vary from $500 for vitamins to tens of thousands of dollars for precious metal investments.

Once a telemarketer has hooked a victim, it will frequently attempt to resell that victim repeatedly through further false promises. It will also sell the name and telephone number of the consumer to other telemarketers, and it is not unusual to see a consumer who has been victimized by multiple telemarketers.

If the consumer is fortunate, he or she will receive inferior, overpriced products. In many cases, he or she will receive nothing at all.

Boilerroom telemarketing is a difficult problem for State law enforcement. These operations are cheap, and they are mobile. A boilerroom essentially requires only leased office space and leased telephones. The most unscrupulous operators may not even bother to purchase the products that they supposedly sell. If the state prosecutes or threatens to prosecute these operators, they simply move to another state and begin again.

Since boilerrooms normally do not solicit citizens of their own states, this fraud is a national rather than a local or State problem.

Now Senator Bryan, as you pointed out before, Nevada and particularly southern Nevada, the Las Vegas area, used to be a center for boilerroom activity. Over 50 percent of all complaints we received in 1987 involved telemarketing, and the percentage went up in 1988. In Nevada, consumer complaints about telemarketing have been over seven times greater than those concerning new and used car sales. Almost all of these complaints are from nonresidents who are victimized by Nevada boilerrooms.

In 1989 Nevada adopted a statutory licensing scheme for telemarketers. Under the current Nevada statute, telemarketers must obtain a restricted license from the state. As part of the licensing requirements, the telemarketer must post a substantial surety bond and abide by strict regulations concerning its sales techniques. Conducting a business without the required license in our state is now a felony.

This licensing requirement has further reduced the number of telemarketers that we currently have operating; however, few of the telemarketers driven out of Nevada have actually gone out of business. Most have simply moved to other states and resumed their operations.

I note with interest, Senator McCain, that the figures went from 334 complaints on contests to 2,500 in a year. I would submit that many of those people just hopped on America West in Las Vegas, and 38 minutes later they are in Phoenix. That is why your numbers have greatly increased.

Forcing boilerrooms out of any particular state is not going to solve the national problem of boilerroom fraud. That is why I continue to say the situation requires a solution on the national level.

S. 2494 is an important step. Both bills are an important step. The Attorneys General and I prefer S. 2494 the way it is written to S. 1441.

In addition to giving the Federal Trade Commission broader power to combat telemarketing fraud, the bill allows State Attorneys General to proceed under the Federal act. We submit this would greatly expand the resources of the FTC by allowing the Attorneys General of all 50 states to combat telemarketing fraud on a national level.

The proposed legislation would increase the efficiency of the actions of each State Attorney General. Presently, each of us is limited to bringing actions under State law in State courts. Since the State court's power ends obviously at the state boundaries, the telemarketer can avoid the action of any one state simply by changing locations.

S. 2494 would allow a State Attorney General to seek relief against fraudulent telemarketers on a national scale in the Federal courts. For essentially the same effort to drive a fraudulent telemarketer out of his state, an Attorney General could halt the telemarketer's activities in all 50 states.

Now on a technical point, I would suggest that change in the language in paragraph 4(a)(7) of S. 2492. As it is currently drafted, this provision could be read to require notice to the Federal Trade Commission and an opportunity to intervene in State law actions brought in State court. I would just suggest that the language of this paragraph be clarified to specifically state that the notice, intervention and removal provisions apply only to State actions brought under S. 2494 or S. 1441 or whatever we eventually come out with.

State and Federal agencies have been working together to combat telemarketing fraud, and the proposed legislation would encourage even greater cooperation in this area as it permits the states and Federal agencies to share both information and responsibilities in addressing telemarketing fraud. It promotes the required coordinated national effort to address this problem. The bill would allow the states and the FTC to divide their workload and target specific fraudulent telemarketers. This cooperative effort would drive many fraudulent telemarketers out of the marketplace, and that is the goal that we are all seeking.

I also would like permission, Mr. Chairman, to make part of the record the written testimony of Attorney General Ken Eichenberry of Washington, who would liked to have been here today but was unable to do so.

Senator BRYAN. That will be made a part of the record.

Thank you very much, Attorney General McKay.

As you have gathered from the colloquy between the subcommittee and the previous witness, there are provisions which are contained in our approaches which I would characterize as the harassment protection provisions; that is, indicating to the FTC that rules would be appropriate with respect to the cooling off period as I have characterized it, the time of the day that these calls can be made, requirements that shipments be made within a certain period of time, and other ancillary things.

Chairman Steiger suggested that she did not think that was as much of a problem. I do not want to put words in her mouth, but she downplayed that. Give us your sense. You have been out there in the front line. Are these kinds of things helpful in your judgment, particularly the cooling off period?

Mr. McKAY. The suggestions that are made in your bill would be very helpful from our point of view, from a law enforcement viewpoint. It sets the parameters. Those people who operate outside of that obviously are the ones that are not legitimate telemarketers anyway, and it really does set decent parameters.

Senator BRYAN. So I take it, then, that from the point of view of the Attorneys General you would like to see the FTC develop some rules in those areas that would be subject to the joint enforcement of the concept that is incorporated in these bills?

Mr. McKAY. We would certainly be supportive of that approach, Senator.

Senator BRYAN. Talk to me for a moment, if you will, about the Federal cause of action which is created and how that helps you. I have heard from your national office, and I know that you are supportive of it, but maybe you could for our record here give us a specific situation or a hypothetical case in which the ability to go into Federal court promptly with the Federal cause of action gives you an additional remedy. Where as a practical matter does that really help you to move into an area where right now you are handicapped or limited?

Mr. McKAY. Where Nevada's reputation suffered for a while back in 1986 and 1987 because we had so many telemarketers operating, we were not necessarily aware of that until after the fact. So this would allow the Attorney General of Minnesota, for example, or the Attorney General of Arizona who became instantly aware of his citizens being solicited to go into court under your venue provisions and stop that activity not only in Nevada but anyplace else where they reach out to.

So it gives us the broad national reach that we currently do not have and that we can only put into effect by calling our colleagues and doing it on a state-by-state basis.

Senator **Bryan**. You have a jurisdictional predicate as the state that is the recipient of the calls that come from an out-of-state destination, I take it, under the venue provisions?

Mr. **McKay**. That is correct. That is certainly how I read the bills.

Senator **Bryan**. There has been, as you have gathered here during the course of this testimony, at least a difference of approach: You made reference to the deputized approach in your testimony; and the ability to go in directly after or concurrent with giving notice.

Discuss that with us, if you will, and in terms of why you prefer the approach that we have outlined in our bill as opposed to the deputized approach which appears to be the preference of Chairman Steiger and the Commission.

Mr. **McKay**. I can understand that from Chairman Steiger's point of view because it would allow the commission to control any activities in the area of litigation involving the rule-making or Federal cause of action, and we certainly would welcome the deputization process. However, we also think we ought to be able to act independently to enforce the law because traditionally, at least, the states have been able to act in a much more expeditious fashion than the Federal Government has been. That is just kind of the nature of the systems, I believe.

So, while we welcome the deputization process, we certainly do not want to submit each state Attorney General to the process of the FTC because it becomes burdensome and might create problems for us within our own jurisdictions because we do not act quickly enough.

Senator **Bryan**. And I, as I assured her, imply no criticism of her. I would agree with your observation that I think there has been a change in attitude since she has become Chairman of the commission. But, of course, you never know prospectively who may occupy the position and who has a different approach and a different relationship with all of you in the National Association of Attorneys General.

Let us talk for a moment. If you had to go through the process of requesting, and assuming again that there was a totally cooperative attitude at the Federal level as evidenced by Chairman Steiger's point, what kind of time, what kind of resources do the FTC offices have?

In the states we all know it takes a little while for the Federal Government to act, and nobody has ever applauded our actions at the Federal level as having moved swiftly when it comes to any enterprise of significant importance. What kind of time does it take?

Mr. **McKay**. I would have to defer to the FTC, but I would expect it would take—you know, we are talking about weeks if not months to be able to get that process functioning and operating, assuming you have a cooperative commission, which we do now. And I do need to reiterate that there in the past was an adversarial relationship between state law enforcement and the FTC which was as unhealthy a situation as you could have, and there is no guarantee that that will not happen someday in the future.

Senator BRYAN. The point I am trying to make, it is not as if you just make a phone call to the Las Vegas office of the FTC and say look, we kind of need to come by and get deputized this afternoon. It is more complicated than that in terms of the mechanics of the process as opposed to the attitude.

Mr. MCKAY. Mr. Chairman, it took about ten weeks for me to become deputized as a Special U.S. Attorney on a particular matter we did. Now, whether it would take that long with the FTC, I do not know. But certainly in the area of telemarketing fraud, any type of fraudulent activity, time is of the essence as you indicated before.

Senator BRYAN. Thank you very much for your testimony. I will defer now to Senator McCain for some questions.

Senator MCCAIN. Thank you, Mr. Chairman. Thank you for being here, Mr. McKay. I appreciate all that you have done as a good neighbor to our state. I appreciate a lot of the cooperation that has existed between Arizona and Nevada.

As I mentioned earlier, I believe that Senator Bryan and I can work out differences that we have in our respective bills on the definition of telemarketing and other issues. As you know, the legislation I have proposed expands the FTC's ability to attack different kinds of fraud as well. Do you have any problems with the rest of my bill that expands the FTC's tools in other areas of fraud that exist today?

Mr. MCKAY. Senator, I am from a state like yours, as you know, that has a burgeoning population, and we are experiencing the same problems you are in Arizona. So, no, I think the more specificity we have in those areas, the more beneficial it is for those of us who have to enforce the laws and try and stop the type of fraudulent activity that you are talking about.

Senator MCCAIN. I am told that those who operate consumer frauds often target senior citizens. Does your experience bear this out?

Mr. MCKAY. Absolutely.

Senator MCCAIN. Could you make a rough guess as to what percentage of the fraud in your state is directed against seniors?

Mr. MCKAY. A ballpark figure would be probably 55 to 65 percent.

Senator MCCAIN. I am concerned about the aspect of allowing private rights of action and state action against fraud in Federal court. I certainly would not want us to characterize this legislation as "Son of RICO." What assurance do we have that state officials and private parties will not go overboard in deciding what is fraudulent in telemarketing? How do we know that plaintiffs under such a bill would not at some point ask a Federal court to declare the delivery of cold pizza constitutes fraudulent telemarketing?

Mr. MCKAY. Well, to answer the second part of your question first, Senator McCain, there is a jurisdictional, monetary jurisdictional threshold of $50,000 under a private cause of action that would eliminate any such action as you just described.

I believe as to state officials acting overzealously all I can do is tell you that I think both myself and all of my colleagues in the other states take our responsibilities very seriously. We only target what we consider to be serious violations of the law and fraudulent activities. And quite frankly, we do not have time to mess around with the other stuff, and I would just defer to Congressman Luken's testimony that no examples have been given to him to date of those concerns.

Senator McCAIN. Who should define what constitutes fraudulent telemarketing in the first instance, state courts, Federal courts, the FTC or Congress?

Mr. McKAY. As any person who is required to enforce the law, the better definition we have, the most specific definition is the easiest for us to work with, so we certainly would work with this committee in establishing the parameters of the definition of telemarketing fraud.

Senator McCAIN. It seems to me that criminal sanctions may be more of a deterrent than that which would result from civil litigation. How many criminal actions for fraud has your state brought in the past year?

Mr. McKAY. I do not know the answer to that question, but not very many.

Senator McCAIN. Because?

Mr. McKAY. We just find it a lot easier, quite frankly, to go in. The burden of proof is less for us, and we can get the business shut down through injunctive relief, and that is the primary function. That is the first thing we want to do is to stop the operation.

Senator McCAIN. I thank you very much, Attorney General McKay. Again, I appreciate your very fine testimony. I hope that we can work out whatever differences that remain so we can ease this terrible burden on the citizens of both our states and other Americans. Thank you Mr. chairman.

Senator BRYAN. Thank you very much, Senator McCain. Attorney General McKay, exercising the prerogative of the Chair, one of your responses elicited from a question that Senator McCain had dealt with the definition of fraud. As you probably know from looking at the other testimony, that has been a concern raised by some of the witnesses who are going to be testifying later. I would like to ask you to work with the staff both in Nevada and nationally and working with our subcommittee staff as to what is an appropriate definition. You have indicated that you think your job and the Attorney General's job would be easier if you had a definition.

As you know, the bill that we have offered does not provide a definition as such, and we want to be helpful rather than just throwing it out there without any guidelines if you think that would be helpful. So, let me ask you to work with us on that, coming up with a definition. As you know, I have asked Chairman Steiger as well to come up with a definition she believes would be workable.

Mr. McKAY. Senator, certainly both those of us in Nevada and the national association will work with you at your convenience and direction.

Senator BRYAN. Good. Thank you so much. We do appreciate your coming back. I look forward to continuing to work with you and the national association.

Mr. McKAY. Thank you very much.

Senator **Bryan**. Our first and only panel, other than the distinguished witnesses who have preceded them this morning, will consist of Ms. Jane King, Fairfax County, Virginia, Office of Consumer Affairs, and she speaks on behalf of the National Association of Consumer Agency Administrators. Mr. Richard A. Barton. Mr. Barton serves as the Senior Vice President for Government Affairs, Direct Marketing Association. Mr. Richard Collier, who is Director of Special Projects, MasterCard International, Inc., and Mr. James Santini, a former member of the Congress and a Washington representative speaking on behalf of the National Tour Association.

Ladies and gentlemen, welcome to the subcommittee hearing this morning. We are happy to have you here. Once you are comfortably seated and are ready to proceed, we would invite Ms. King to begin our testimony from this panel.

STATEMENT OF JANE KING, FAIRFAX COUNTY, VA, OFFICE OF CONSUMER AFFAIRS, ON BEHALF OF THE NATIONAL ASSOCIATION OF CONSUMER AGENCY ADMINISTRATORS

Ms. **King**. Mr. Chairman, distinguished committee members, my name is Jane King. I am here on behalf of the National Association of Consumer Agency administrators or NACAA. NACAA is a membership organization for some 120 chief executive officials of local, state and Federal consumer protection agencies. NACAA member agencies in most states and locales are in the front line in the war against telemarketing abuse.

We have had the opportunity to review the working draft of April 17, 1990, from Senator Bryan's staff. While we have not yet presented the details of the proposal to the NACAA executive board, I am authorized by NACAA's President to speak for the membership in supporting this proposal today.

During the past years we have testified regarding several proposals in the House of Representatives to regulate telemarketing. Due to the pervasiveness of abuse in this industry, which some estimates place at more $1 billion in fraudulent sales per year—and we all know that it is much more than that—we were initially supportive of the House proposals. However, they have now been so weakened by various lobbying interests that we are close to withdrawing our support and opposing H.R. 1354 since we believe it would only provide the consuming public with a false sense of security and thereby serve to exacerbate the problem.

However, the Senate working draft we have reviewed does not contain the same fatal flaws as the House bill. The Senate proposal does not provide exemptions for any segment of the telemarketing industry, nor should it. The Senate proposal does not require that 30 days' advance notice be given to the Federal Trade Commission before a state Attorney General may file suit under Federal law, a provision which gives con artists ample time to move their location and begin operating elsewhere. The Senator proposal also does not contain the inadequate and legally unintelligible phrase "fraudulent device" found in the House bill.

We do have some recommendations, however, regarding this proposal which we hope you will consider. Section 4(a) of the April 17 draft deals with actions by state Attorneys General. Subsection 5 of section 4(a) states that "Nothing in the proposed act would prevent the state Attorney General from exercising his or her investigative powers under state law." We suggest that this be amended so that other state and local officials are similarly not prevented from exercising their powers and duties under state and local law.

For example, in Georgia the administrator of the Governor's Office of Consumer Affairs rather than the Attorney General is the state official who is authorized by law to conduct consumer protection investigations into alleged unfair and deceptive activity, to administer oaths and affirmations, and to compel the attendance of witnesses or the production of evidence. Similar arrangements exist in other states and locales. By not including other authorized states and local officials in subsection 5 it could be interpreted as preventing such officials from exercising their legal authority.

Also, subsection 6 of section 4(a) states that authorized State officials shall not be prohibited from proceeding in State courts regarding violations of general anti-fraud statutes. This, though a technical point, is a very important one. It would be more accurate terminology to include unfair and deceptive acts and practices statutes along with anti-fraud statutes.

There is a legal distinction between these terms. Unfair and deceptive acts and practices statutes which exist in all 50 States are usually administered and enforced by local and State consumer officials, while anti-fraud statutes may not be. Moreover, the elements of proof under the two types of statutes differ.

Additionally, State and local officials may also act under State and local rules, regulations or ordinances. The language of the bill should specify that officials so acting will not be prohibited from doing so.

Subsection 7 of section 4(a) presents the biggest problem with this bill. As presently drafted, this section could be construed to require a State official proceeding under State law in a State court regarding any unfair, deceptive or fraudulent activity to give prior written notice of his or her intent to do so to the FTC, and would allow the FTC to intervene in any such State proceeding. This would be an unconscionable intrusion upon State authority.

Requiring advance notice, even in telemarketing cases, is like telling a soldier under attack that he may not fire back until he is sent written notice to the White House of his intentions. There is no historic precedent for giving the FTC authority to interfere in cases in State courts under State law, and there is no good reason for suddenly giving the Commission that authority now.

A decade has just ended in which consumer protection was left almost entirely up to the States. To plunge into the unexplored waters of Federal intervention in State consumer protection matters at this juncture is neither warranted nor wise. Even if the Congress were to take this giant leap and allow the FTC to intervene in such proceedings, the bill should state that failure to notify the Commission shall not constitute a defense to the State action.

If this is to truly be a consumer protection measure, the Congress must avoid obstructing State and local consumer protection agencies in the performance of their duties. We do not believe that this was the drafter's intent, and we strongly urge that subsection 7 be substantially redrafted. Except for these points I have just mentioned, we find this proposal to be a strong, viable and positive step in the war against telemarketing fraud.

Though S. 1441 addresses important issues for consumers, the long-term health care insurance and life care provisions are generally out of the purview of most NACAA members. We would like, however, to reserve the right to comment further that the jurisdiction of the FTC vis-a-vis the Attorneys General in 1441 also fails to address the role of NACAA members in some States and may pose severe administrative problems that may also slow prosecution.

Thank you for this opportunity to appear before you.

Senator **Bryan**. Thank you very much, Ms. King. We appreciate very much your testimony. We will next hear from Mr. Barton.

STATEMENT OF RICHARD A. BARTON, SENIOR VICE PRESIDENT FOR GOVERNMENT AFFAIRS, DIRECT MARKETING ASSOCIATION

Mr. **Barton**. Mr. Chairman, Senator McCain, it is a real pleasure to be here testifying before you today on this very important subject.

The Direct Marketing Association is a national trade association with approximately 3,000 domestic corporations as members that are involved in all forms of direct marketing, and telemarketing is a very important part of the business of our association members.

We have, I believe, a very strong reputation in the field of working hard to develop ethical guidelines for the practices of all of our members in all of our areas of direct marketing, and this certainly is also the case in combatting telemarketing abuse—what we like to call "telefraud" rather than "telemarketing fraud"—through our ethical business guidelines, through our Ethical Business Practices Committee, which uses peer pressure to enforce our ethical guidelines, through our cooperation on a very deep level with organizations such as the National Association of Attorney Generals, the Federal Trade Commission, the National Consumers League and the Alliance Against Telemarketing Fraud.

I would like to say very quickly here that we have copies of two major consumer pamphlets, which we were supposed to include with the testimony, and I will include it now, after this—our guidelines for telephone shopping and also our own ethical guidelines for marketing by telephone.

Senator **Bryan**. Those documents or publications will be made a part of the record, by reference Mr. Barton.

Mr. **Barton**. Thank you, sir, and next time we will supply them with the testimony, if there is a next time.

We of course feel that it is of very strong interest, not only to consumers but the legitimate part of the telemarketing community, to promote legitimate telemarketing and do the best we can to eliminate fraud, and we work very hard at it with the people that I have been talking about.

We think that your bill and Senator McCain's bill is an improvement over Congressman Luken's bill, even though I have to underline that we respect very much the work that Congressman Luken has done in this area and that his Subcommittee and Subcommittee staff has done in this area. We all recognize, I think, that it is important to have some new legislation to combat telemarketing fraud. We sometimes disagree on the direction that that legislation should take.

I guess if we have a general philosophy that we would like to state here, is first we believe that we need strong telemarketing fraud laws and regulations and enforcement on both the State and Federal level, but in line with the State from which I come—Virginia—we believe that the States ought to enforce strong State laws and the Federal Government should enforce strong Federal laws.

Not that there should not be cooperation, and a great deal of cooperation back and forth, but that we have concerns when we begin to give a broad grant of enforcement of Federal law to State Attorneys General. It is not that we think that Attorneys General are reckless. I think somebody quoted me as saying ""rogue Attorneys General" which I do not remember saying, but I will admit to that, perhaps. It is that we are facing the fact in some of these bills that the telemarketing industry, and the legitimate telemarketing industry, is going to be looking at 50 different interpretations of Federal legislation and application of Federal legislation, and we think that has the potential for a great deal of confusion in the telemarketing business and perhaps a certain amount of injustice, though I do not want to emphasize that too long.

We think this is particularly true because, as you have pointed out, and the Federal Trade Commission pointed out, there is not really a definition of a fraudulent act or a practice, and we believe that it is important that we try to, if we are going to pass legislation of this nature, that we do try to come up with some sort of definition so that we can have some greater consistency in the application of law if we do not have this.

We believe that your approach, Senator Bryan, is certainly a good and a legitimate one, and we agree, I think, with Miss King and with the Federal Trade Commission that it is a better and more comprehensive approach than we now have in the House legislation, but we would rather move more in the direction of Senator McCain's bill, where you would deputize, and we would hope it would be done very quickly, State Attorneys General by the Federal Trade Commission, and we are glad to see the Commission agrees with us.

We also question the need for a new private Federal cause of action. Consumers can now bring suit under State law, but if we are going to have such an action—a private cause of action—we would suggest that the plaintiff—each plaintiff in the suit would meet the amount in controversy standard for asserted damages so that we could avoid the nuisance claims or class actions in which a consolidation of very small claims would allow us to tie up the courts and perhaps some legitimate telemarketing firms.

We would also suggest that attorneys fees and court costs should be available to the prevailing defendants as well as the prevailing plaintiffs, which would also further deter nuisances.

You have also discussed here the definition of "telemarketing," which we think needs to be tightened. There is no definition of "telemarketing." We would want to clarify what is meant by "significant use of phones," and we would be glad to work with the Subcommittee staff on this, and we also think it would be appropriate to exclude at least unsolicited in-bound telemarketing calls from the scope of the bill if these calls are based on a preexisting relationship.

A lot of very legitimate telemarketing goes on with 800 numbers, in which you are ordering from catalogues from which you have already had a preexisting relationship, and we really see no reason to bring that kind of telemarketing call under this bill. It would just make things a lot simpler. We would also suggest the same thing for any telemarketing call in which there is a preexisting relationship, if we could come up with a good definition of a preexisting relationship.

Finally, in connection with the proposals for rule-making in the areas such as hours of calling, cooling off period and other areas, we agree with the Federal Trade Commission. We do not think that such regulation would necessarily go to the root cause of telemarketing fraud.

Some fraudulent operators would pay no attention to it and disappear, but the intriguing thing, as the Chairman of the Federal Trade Commission indicated, a lot of telemarketing fraud operators very rigorously would obey these regulations, and I do not think we would be much ahead by adopting them.

That being said, we agree with your approach in this bill, in that you ask the Commission to consider regulations in this area rather than requiring the Commission to come up with specific regulations, and the reason for this is that even though it is deceptively simple to say, as our telemarketing guidelines or ethical business practices say, that you should have a cooling off period, it is another thing to require in every telemarketing transaction that there be a cooling off period, because there may be some areas—for example the buying of stocks, insurance policies, in a legitimate way, food, for example—in which a cooling off period would not be particularly helpful to the consumer.

So the way your legislation drafts it is that we would consider this in a rule-making process and I think it is the proper approach to take, and I think we could work with the Commission in developing regulations in these areas that would, I think, be fair to legitimate telemarketers and still achieve many of the goals that you want to achieve.

We want to work with you and the staff of the Subcommittee in developing a good bill, and we hope that we are going to get some good telemarketing fraud legislation this year.

Thank you.

[The statement follows:]

PREPARED STATEMENT OF

RICHARD A. BARTON
SENIOR VICE PRESIDENT FOR GOVERNMENT AFFAIRS
DIRECT MARKETING ASSOCIATION

Mr. Chairman and Members of the Subcommittee:

My name is Richard A. Barton, and I am the Senior Vice President for Government Affairs of the Direct Marketing Association.

The Direct Marketing Association ("DMA"), with offices in New York City and Washington, D.C., is a national trade association representing over 3,000 companies and organizations that market products and services through the mail, electronic and print media, and through telemarketing.

The DMA embraces a broad range of companies and organizations that share an interest in the two proposals for telemarketing legislation which are pending before this Subcommittee. Some DMA members, such as L.L. Bean, utilize only "in-bound" telemarketing, as an order-taking service for customer convenience, while some, such as Olan Mills, use "out-bound" telemarketing, as a means to sell their products and services. Other DMA members, such as DialAmerica Marketing, are service bureaus which advertise and sell the products and services of other companies through telemarketing.

These DMA members -- as well as the many charitable, religious, educational, and political organizations that are DMA members and widely make use of telemarketing for fund-raising campaigns -- have an important stake in supporting efforts to combat telemarketing fraud. At the same time, they want to ensure that such efforts avoid unnecessary and overly restrictive measures which would prohibit or interfere with legitimate telemarketing activities.

DMA WORKS ACTIVELY TO COMBAT TELEMARKETING ABUSES

Telemarketing is a very important tool for DMA members. As you will note in the attached booklet, "Telemarketing Today: The Right Connection", companies in nearly every sphere of the business world utilize telemarketing to sell products and services. Today, more than two million people are employed in the telemarketing industry. In 1987, according to Direct Marketing magazine, business expenditures in the telemarketing industry totaled $43.4 billion.

The public's confidence in the legitimacy and reliability of telemarketers is essential to the continued success and growth of this form of marketing. Obviously, legitimate telemarketers have a strong incentive to support reasonable government regulatory and law enforcement efforts to combat telemarketing abuses, as well as to mount their own initiatives to maintain the integrity of common telemarketing practices.

Recognizing the need to guard against potential abuses in the telemarketing industry, the DMA has been actively working with the Federal Trade Commission ("FTC"), the National Association of Attorneys General ("NAAG"), the National Consumers League ("NCL") and other interested parties to develop consumer education and other programs to rid the industry of fraudulent telemarketers.

In January 1987, the FTC and NAAG announced the development of a coordinated federal-state campaign against telemarketing fraud. The main goal of the campaign was to establish a national telemarketing fraud database clearinghouse. The DMA's Ethics and Consumer Affairs Department actively participates in this database by forwarding complaints which appear to involve fraud.

In yet another effort to cooperate with interested parties in guarding against fraudulent telemarketing practices, the DMA joined a coalition against telephone fraud sponsored by NAAG. The main purpose of this coalition is to identify problem areas associated with fraud in the telemarketing arena and to propose effective, preventive measures.

The DMA recognizes that the best weapon against any fraudulent business conduct is an informed and vigilant consumer public. To this end, the DMA has committed extensive association resources to educating consumers on how to protect themselves in their business dealings. The DMA has produced and distributed consumer tips to action line reporters, and has developed and distributed important consumer pamphlets such as the Guidelines for Telephone Shopping (see attached). Additionally, the DMA has participated in the work of the Steering Committee of the National Consumer League's Alliance Against Fraud in Telemarketing.

The DMA's Ethics and Consumer Affairs Department also promotes industry self-regulation through its direct marketing guidelines, and offers consumers their own option for self-help through its

Telephone Preference Service. Through this service, offered free to consumers, telemarketers will remove the name of any consumer from their telephone marketing lists upon the consumer's request.

The DMA's Committee on Ethical Business Practice was established to investigate and examine offerings throughout the direct marketing field. This is done in an effort to improve business practices within the direct marketing industry as well as to provide additional consumer protection. Complaints are referred to the committee by consumers, action line reporters, and industry members. In cases involving possible law violations and a lack of company cooperation, the complaint files are turned over to the FTC, the office of the attorney general in the marketer's home state, the U.S. Postal Inspection Service, or other law enforcement agencies.

For a number of years, in its "Guidelines for Telephone Marketing" (see attached), the DMA has encouraged telephone marketers to abide by the FTC's Mail Order Merchandise (30-Day) Rule when shipping prepaid merchandise. Several months ago, when the FTC published a proposed rule which would apply the 30-day rule to cover shipment of prepaid merchandise ordered by telephone, the DMA filed comments and testified reaffirming its view that, in principle, the rule should apply to telephone transactions.

THE DMA'S CONCERNS REGARDING PENDING FEDERAL LEGISLATIVE PROPOSALS

The DMA looks forward to further cooperation with interested parties to combat fraudulent telemarketing practices; however, we urge Congress to proceed cautiously with new legislative proposals which would change the legal landscape to expand law enforcement efforts in this area. Overly broad and restrictive legislation may impair the ability of honest merchants and marketers to efficiently provide needed goods and services to the American people, while proving to be unnecessary or ineffectual supplements to existing law enforcement authorities and capabilities.

We appreciate the care taken by both the Chairman and Senator McCain in attempting to narrowly-craft their respective proposals. Although they significantly differ in a number of their provisions, S.2494 and S.1441, taken in their entireties, are each preferable to H.R. 1354, the broadly-drafted bill approved by the House Energy and Commerce Committee last fall.

Nevertheless, we have certain concerns regarding both Senate bills which we would like to share with you at this time. We offer the following comments as a first step in what we hope will be a constructive and mutually beneficial dialogue between the DMA and the members of this Subcommittee in shaping any new telemarketing legislation:

Definition of "Telemarketing"

Subsection 2(4) of S.2494 defines "telemarketing" to mean "a plan, program, or campaign conducted to induce purchases of goods or services by significant use of one or more telephones through interstate voice telephone calls," excluding from the definition "other use of a telephone in connection with business or personal transactions."

The DMA believes that this definition is preferable to the one provided in subsection 5(e)(2) of S.1441 because it is more precise in its terms. However, we believe that further clarification of the definition is advisable for the purpose of more sensibly shaping the scope of "telemarketing" activity that the bill intends to reach.

Specifically, it is unclear what would constitute "significant" use of telephones under this definition. Although the qualification would appear to be intended to ensure that an activity is not deemed "telemarketing" simply because it involves some use of telephones for marketing purposes, clarification is necessary so that the scope of the definition may be clear.

In clarifying this definition, we believe it would be appropriate to exclude "in-bound" marketing, or "order taking over the telephone," where the consumer initiates the telephone call to the marketer. We also believe that "out-bound" calls should be excluded where there is a preexisting relationship between the marketer and the consumer. This is because where the consumer voluntarily initiates the transaction, or when the consumer has had prior dealings with the marketer, the marketplace and existing law provide more than adequate safeguards against fraud, rendering special legislation and rules unnecessary.

FTC Rulemaking

In view of the renewed interest and activity at the FTC with respect to combatting fraudulent telemarketing activities, the DMA questions whether there is any need for additional FTC regulations governing telemarketing. However, if Congress believes that new FTC rules are necessary, we believe that both S.2494 and S.1441 take the sensible approach in permitting the FTC to decide what further rules are necessary or appropriate, rather than mandating adoption of specific rules as would H.R.1354.

We believe that the approach taken in H.R. 1354, which mandates the FTC's adoption of specific rules on delivery, cancellation, hours-of-the-day restrictions, and record-keeping, seriously underestimates the complexity of both the issues and the legal and policy considerations involved in these areas.

By directing the FTC to "consider" the rules specified in subsection 3(a) of S.2494 and in subsection 5(b) of S.1441, both Senate bills leave requisite flexibility for the FTC to decide, on the basis of an adequate public record and in the exercise of its expertise, whether particular regulations in these areas are necessary and, if so, what form and scope they should take.

For the same reasons, however, we believe that Congress should not mandate that the FTC issue its rules within a specified period after enactment of the legislation. The expedited rulemaking procedure was designed to be used by the Commission when dealing with relatively simple, non-controversial issues. Such is not the case in the areas referenced in the two Senate bills.

State Attorney General Action

The DMA respects the right of every State Attorney General to take legal action against intrastate telemarketing activities pursuant to State laws that address fraud. However, the DMA has serious problems with any legislation which would expand the jurisdiction of State law enforcement officials by authorizing them to file suit in federal court against interstate telemarketing activities on the basis of their own interpretations of FTC rules and an undefined concept of "fraudulent act or practice."

Far from creating national standards aimed at more effectively extirpating interstate telemarketing fraud, proposals like the one in section 5 of S.2494 and a similar proposal in H.R.1354 will serve only to create confusion and uncertainty on the part of legitimate marketers as to what is or is not permissible interstate telemarketing activity. They create the possibility, if not the probability, that state authorities may interpret the FTC's rules in ways which the FTC itself did not intend. Certainly, the FTC should be vested with the exclusive power to enforce its own rules;

and, as we have stated, we believe it has abundant authority to act not only with respect to rule violations generally but with respect to telemarketing fraud.

S.2494 would allow any state attorney general to bring a civil action in a federal court by merely alleging that residents of the state "may be threatened or adversely affected because any person... is about to engage in" telemarketing which is a fraudulent act or practice or is a violation of FTC rules, orders, or regulations. Although the bill would require the State official to notify the FTC of such action, such notice is due only after the action is commenced. This standard does not ensure that there is a meaningful nexus between the marketer and the state, and the notice requirement merely facilitates the FTC's right to intervene in the suit once it has been filed.

We do not see any valid reason why State Attorneys General need authority to bring actions under federal law. Generally speaking, we have seen no evidence that they lack adequate authority under State law to pursue intrastate activities, or that the FTC is unable to pursue fraudulent interstate telemarketing activities with its existing authority and resources.

It is possible that there may be rare emergency situations where a State Attorney General would be capable of acting more quickly than the FTC to enforce federal law. Although we cannot visualize such circumstances, we believe that such a need would be adequately addressed by the kind of deputization proposed in subsection 4(e) of S.1441. This would not require the kind of full-blown delegation of law enforcement authority proposed in both S.2494 and H.R.1354, yet the State official would be authorized to act and the FTC, with its internal procedures and control systems, would retain authority over legal actions determined in advance to be in the public interest.

Section 3(d) of S.2494 deepens our concern over the proposed cause of action for State Attorneys General because it appears to permit State preemption of FTC rules with respect to interstate telemarketing activities. Although the language of the bill does not clearly compel this interpretation, we believe that it is sufficiently ambiguous as to require clarification of the drafter's intent.

In addition, constitutional and jurisdictional questions are raised by these provisions concerning the scope of relief which a State Attorney General may obtain. It would appear, for example, that the bill allows for relief relating to persons outside the attorney general's state and makes such relief applicable to conduct outside the state. It is not clear how this may be accomplished without running afoul of the Appointments Clause and due process requirements.

A related problem arises with respect to the power of state authorities to sue for conduct which constitutes a "fraudulent act or practice." We take this language to establish a more stringent standard than the one imposed upon the FTC under Section 5 of the

Federal Trade Commission Act. In establishing a more stringent standard, the Act takes a step in the right direction because it is intended to permit state authority litigation to be initiated only when there is genuine abuse, virtually amounting to quasi-criminal fraud. However, the bill fails to address the question of what law is to be applied in determining whether the conduct complained of by a state attorney general "is a fraudulent act or practice." This is a question of great importance since the bill would allow state attorneys general to proceed against marketers who do not have a substantial presence within the state initiating the litigation. To the extent that the conduct alleged to be a fraudulent act or practice is to be judged under the laws of the state which has initiated the complaint, that bill would serve only to permit the attorneys general to proceed in federal rather than state court under laws which already exist in that state. To the extent that the bill is intended to allow the attorney general of one state to impose its notions of what constitutes a "fraudulent act or practice" upon a marketer who operates from another state, there are very serious choice-of-law and constitutional questions involved.

Thus, both in concept and particulars, the provisions authorizing state law enforcement authorities to proceed against out-of-state telemarketers in the federal courts are extremely troubling to the DMA.

Private Actions

In the long history of the Federal Trade Commission Act, the courts and the Congress have staunchly resisted the creation of a private remedy for violations of that Act and the Commission's rules created under it. There are good reasons for this, and those reasons apply here as well. With virtually nothing to be gained (a private citizen could always bring an action in state court) and much to be lost (the further burdening of an already overburdened federal judiciary), S.2494, like H.R.1354, would potentially allow an unlimited number of lawsuits involving matters which may have little more than nuisance value. We do not see any justification for creating the private cause of action as proposed.

If, however, Congress were to create a private cause of action along the lines proposed in S.2494, we would hope that our previous comments regarding the absence of a definition for "fraudulent act or practice" would be heeded. In addition, we would note that the "amount in controversy" jurisdictional standard for such actions should be clarified so that it is clearly understood to require satisfaction by each individual plaintiff in a suit. Finally, with respect to costs and attorneys and expert fees, the DMA does not believe that such a provision is necessary or desirable in the bill. However, if such awards are to be authorized, we believe that they should not be available only to a prevailing plaintiff but should be available to a prevailing defendant as well.

Conclusion

There are a number of other technical and legal issues in both Senate bills which we have not addressed in this testimony, but which need further exploration. Our basic conclusion is that telemarketing fraud is a major consumer problem and it is a problem for business as well. Although the fraudulent telemarketers represent only a small minority of telemarketers, they do a great deal to damage legitimate businesses. They steal sales based upon deception and poison the public's perception of telemarketing generally. The DMA is very interested in assisting the Congress in its efforts to combat the problem of telemarketing fraud. We look forward to working with this Subcommittee to produce a law which is effective and fair.

Senator BRYAN. Thank you very much.

Mr. Collier, we will hear next from you, sir.

STATEMENT OF RICHARD COLLIER, DIRECTOR, SPECIAL PROJECTS, MASTERCARD INTERNATIONAL, INC.

Mr. COLLIER. Mr. Chairman, my name is Richard Collier. I am Director of Special Projects at MasterCard and I am appearing here today on behalf of both Visa USA and MasterCard International.

MasterCard and Visa appreciate the opportunity to be here to testify before the Subcommittee on the important and growing problem of telemarketing fraud. In addition to my oral testimony, Visa and MasterCard have submitted written testimony which I request be made a part of the record of this hearing.

Senator BRYAN. That will be the order.

Mr. COLLIER. In our written testimony we described telemarketing fraud and its evolution over time. We describe why it is that the banking industry is very much the victim of telemarketing fraud. Indeed, MasterCard and VISA estimate that our financial institution members lose in excess of $200 million per year as a result of telemarketing fraud involving payment by credit card.

The written testimony also describes the extensive and continuing efforts undertaken by VISA and MasterCard and our financial institution members to address telemarketing fraud. We also describe why, despite all of these efforts, sophisticated fraudulent telemarketers continue to gain access to the credit card systems.

For the reasons discussed in our written testimony, we believe that telemarketing fraud losses will continue to escalate without an effective Federal legislative response to this national problem. Accordingly, we support properly structured and focused Federal legislation to address telemarketing fraud. We commend the Subcommittee for considering telemarketing fraud legislation.

I would like to spend the remaining portion of my time today discussing our recommendations for amendments to the telemarketing fraud legislation being considered by the Subcommittee.

Issues relating to the scope of Federal telemarketing fraud legislation are, in many respects, the most important and difficult issues associated with the bills being considered today by the Subcommittee. The legislation is intended to stop fraudulent telemarketers. Accordingly, it is critical to limit the scope of the legislation as narrowly as possible so as not to unduly interfere with legitimate telemarketers and other merchants which have not engaged in telemarketing fraud.

On the other hand, the legislation must not be so narrowly drafted as to provide loopholes to which sophisticated fraudulent telemarketers could escape the reach of the legislation.

For the reasons discussed in our written testimony, we believe that the definition of the term telemarketing in 2494 is more appropriate than a definition of that term contained in 1441. However, we oppose the exclusion in 2494 of intrastate telephone calls. As described in our written testimony, we believe that this exclusion will provide unintended loopholes for sophisticated fraudulent telemarketers.

MasterCard and VISA also recommend, for the reasons discussed in our written testimony, that the bills be amended to exempt from their scope, depository institutions and their affiliates and subsidiaries. These bills also should be amended to provide that Federal bank regulatory agencies are not required to promulgate substantially similar rules to those promulgated by the Commission under these bills, as it is generally required under the FTC Act. Without these amendments, VISA and MasterCard would not be able to support these bills.

Given the problem that the legislation is designed to address, telemarketing fraud, we believe that the section of these bills concerning FTC rule making should be amended to simply require the Commission to adopt rules regarding telemarketing fraud. The specifics of the telemarketing fraud rules should be left to the Commission as the expert agency in this area, to develop and amend, over time as telemarketing fraud evolves.

As for the private right of action, we believe it to be an essential element of any effective Federal response to telemarketing fraud. However, MasterCard and VISA recommend that 2494 be amended to provide that the amount in controversy for an action brought by an organization comprised of financial institution members is the aggregate of the amount in controversy claimed by the individual members of the organization.

VISA and MasterCard also recommend that 2494 be clarified to provide the Federal courts with exclusive jurisdiction of all private causes of action brought under 2494.

Mr. Chairman, let me reiterate what I said earlier. Not withstanding that there are a number of amendments which we believe are necessary for the bills, MasterCard and VISA support properly structured and focused Federal legislation to address telemarketing fraud. We are prepared to direct our Washington counsel, Morrison

& Foerster, to work with the Subcommittee and its staff to develop the legislation that would be the most effective possible in addressing telemarketing fraud.

That concludes my testimony and I will be pleased to answer any questions that the Subcommittee might have on either my testimony today or the written testimony we have submitted. Thank you.

[The statement follows:]

TESTIMONY OF

VISA U.S.A. INC.

AND

MASTERCARD INTERNATIONAL, INC.

MasterCard International, Inc. ("MasterCard")[1] and VISA U.S.A. Inc ("VISA")[2] appreciate the opportunity to testify before the Consumer Subcommittee of the Senate Committee on Commerce, Science and Transportation ("Subcommittee") on the important issue of telemarketing fraud legislation. The Subcommittee is to be commended for considering federal legislation to address the growing problem of telemarketing fraud.

For the reasons discussed in this testimony, VISA and MasterCard support properly structured and focused federal legislation to address telemarketing fraud. We believe that the Telemarketing Fraud and Abuse Prevention Act of 1990, S. 2494, represents an important step toward realizing that goal. However, certain amendments to the bill, which are discussed later in this testimony, must be made before MasterCard and VISA can provide their unqualified support for the bill.

1/ MasterCard is a membership organization comprised of financial institutions that are licensed to use the MasterCard service marks in connection with payment systems, including credit cards.

2/ VISA is a membership association comprised of financial institutions in the United States that are licensed to use the VISA service marks in connection with payment systems, including credit cards.

Description of Telemarketing Fraud

The Federal Trade Commission ("Commission") has estimated that losses due to telemarketing fraud exceed $1 billion per year. These losses most frequently result from telemarketers who fraudulently solicit consumers by telephone and dupe them into purchasing goods or services which are either substantially inferior to those which have been promised or which the fraudulent telemarketers have no intention of delivering.

Although telemarketing fraud can involve almost any type of payment system, a substantial amount of this type of fraud involves the use of the credit card payment system. Notwithstanding the extensive and continuing efforts of VISA, MasterCard and their financial institution members to address telemarketing fraud, which are discussed below, this fraud continues to grow. We will, in our testimony, focus primarily on telemarketing fraud involving credit cards.

The first generation of telemarketing schemes involved the solicitation of a consumer over the telephone, during which time the fraudulent operator obtained the consumer's credit card number. The fraudulent operator subsequently either charged the consumer for products that were materially inferior to those the consumer expected based on representations made during the telephone solicitation or submitted unauthorized charges utilizing the consumer's credit card number. The victimized cardholder generally became aware of the telemarketing scam upon inspecting the products received or upon reviewing his or her credit card statement. Thus, these early telemarketing schemes typically had a relatively short duration because the scheme would become evident during the first or second credit card billing cycle after the cardholder was victimized.

The telemarketing scams perpetrated today have become significantly more sophisticated. Many current telemarketing schemes purposefully are structured to involve significant time delays between the time at which charges are incurred on the credit card and the delivery of the promised goods or services. As a result, such schemes are extremely difficult to detect at their inception and many consumers fail to realize they have been "taken" until a substantial period of time has gone by and the fraud is uncovered. For example, under travel scam programs, the consumer generally is charged for the "bargain" travel package shortly after providing his or her credit card number to the fraudulent telemarketer, notwithstanding that the consumer typically will not attempt to take the trip until several months later. Since a significant amount of time normally elapses between the time charges are incurred and the time the telemarketer is required to deliver goods or services, the fraudulent operator is able to continue this type of scheme for a significant period of time without detection.

Travel scams have constituted a large amount of telemarketing fraud. However, other types of telemarketing fraud also have surfaced in recent years. For example, consumers promised various "prizes," such as cameras, mink coats and television sets, have been deceived into purchasing vitamins at greatly inflated prices only to find that their prizes do not exist or are worth far less than reasonably expected. Other consumers have been offered gold bullion at discount prices, but were told that orders had to be placed and paid for two or three months in advance. Unfortunately, the gold was never delivered. In fact, the scam artists never intended to deliver the gold.

Financial Institution Losses From Telemarketing Fraud

Financial institutions suffer substantial losses when consumers cancel credit card transactions after the financial institution has paid the telemarketing merchant perpetrating the fraud for the cancelled transactions and the financial institution cannot locate or otherwise obtain reimbursement from that fraudulent telemarketer. Although telemarketing fraud may appear "penny ante" when considered on an individual case basis, it clearly is a "large dollar problem" when individual cases are aggregated. In this regard, MasterCard and VISA estimate that their financial institution members lose in excess of $200 million per year as a result of telemarketing fraud schemes involving payment by credit card.

A number of the telemarketing fraud schemes uncovered during the past few years have involved losses in excess of $1 million each. Two banks recently have reported telemarketing fraud-related losses for a one-year period in excess of $2.5 million. Indeed, earlier this year, the Office of the Comptroller of the Currency issued a news release about a national bank whose failure was caused, in part, by telemarketing-related losses. In addition to out-of-pocket losses to fraudulent telemarketers, financial institutions spend millions of dollars each year to review and investigate individual cardholder complaints, process adjustments to cardholder accounts, pursue and prosecute particular telemarketing fraud operations, and combat telemarketing fraud generally. It is clear that the banking industry is very much the victim of telemarketing fraud.

Moreover, telemarketing fraud poses a threat to the very integrity of the credit card systems themselves. The benefits currently enjoyed by consumers, businesses and other participants in this country's credit card system result, in part, from the widespread acceptability and reliability of the systems and the confidence placed in them. Telemarketing fraud is a very real threat to this confidence, which has taken decades to build.

Financial Industry Efforts to Address Telemarketing Fraud.

VISA and MasterCard and their members have been aggressive in their efforts to address telemarketing fraud, and remain committed to pursuing all appropriate measures to combat this growing problem. In this regard, MasterCard and VISA have actively cooperated with federal and state law enforcement agencies and other federal and state agencies to address telemarketing fraud, and will continue to do so. As a result of these coordinated efforts, several cases have been successfully prosecuted in recent years.

VISA and MasterCard also are continuing to educate their member financial institutions and consumers about fraudulent telemarketing practices. For example, MasterCard and VISA have sent several formal communications to their member financial institutions concerning the problem of telemarketing fraud and have prepared a "statement stuffer" for members to distribute to cardholders warning of the dangers posed by telemarketing fraud. VISA and MasterCard also have prepared a crime prevention advertisement and videotape concerning telemarketing fraud.

In addition, MasterCard and VISA have bolstered their procedures to identify businesses engaged in fraudulent practices, including telemarketing fraud, and to deny them access to the VISA and MasterCard credit card payment systems. In this regard, MasterCard and VISA require member financial institutions to investigate merchants applying for entry into the VISA and MasterCard payment systems. Pursuant to these merchant investigation requirements, several procedures must be performed by MasterCard and VISA member institutions before a merchant can be licensed to accept VISA or MasterCard credit cards. At a minimum, before accepting a merchant, a member institution must conduct: (1) a credit check and/or other financial background investigation regarding the merchant; (2) a physical inspection of the merchant's place of business; and (3) a check to determine if the merchant has been previously terminated for fraud or suspected fraud.

Though seemingly straightforward, these screening procedures must be implemented very carefully in order to protect the legitimate interests of honest merchants. As a result, member institutions are required to engage in a delicate balance: on the one hand the member institution must attempt to protect the integrity of the credit card system by denying access to dishonest merchants, while on the other hand the member institution must be cautious so as not to exclude or unduly hinder the activities of legitimate businesses that often rely heavily on the credit card payment systems. This balancing process is particularly difficult when the applicant is a new business with no performance record against which its trustworthiness can be measured.

MasterCard and VISA also independently monitor the chargeback activity of merchants (i.e., the cancellation by consumers of credit card transactions with the merchant), and require member institutions to investigate and address problems if chargeback levels at a merchant are increasing. Member institutions are also fined if a merchant's chargeback level exceeds a reasonable range. Ultimately, VISA and MasterCard, acting independently, have the authority to expel from participation in their respective credit card systems a merchant demonstrating a pattern of abuse of the system, or which has engaged in confirmed fraud. Several telemarketers have been expelled for these reasons to date.

Despite all the efforts of MasterCard, VISA and their members, sophisticated fraudulent telemarketers continue to gain access to the credit card systems. For example, fraudulent telemarketers have established seemingly legitimate businesses, and have operated these businesses in a proper fashion for a period of time in order to gain the confidence of a bank providing credit card payment services, prior to engaging in a large-scale telemarketing fraud operation.

Other fraudulent telemarketers have successfully persuaded merchants with VISA and/or MasterCard contracts to submit the telemarketers' sales drafts into the credit card payment system in the name of that merchant. This practice, which violates MasterCard and VISA rules, is called "credit card laundering." In the case of credit card laundering schemes, the fraudulent telemarketers typically have fled the jurisdiction by the time the fraud is discovered and the merchants through which the credit card charges are submitted often are deluged with credit card chargebacks. (Certain of the sophisticated operators now launder sales drafts through several merchants at once in order to deter detection.) Indeed, in one recent situation, the chargebacks associated with such a laundering scheme resulted in significant losses to the merchant and the bank involved and may have resulted in the bankruptcy of the merchant.

VISA and MasterCard believe that telemarketing fraud losses will continue to mount without an effective federal legislative response to this national problem. State and local enforcement agencies, often with the assistance of MasterCard, VISA, or their member institutions, have initiated actions against fraudulent telemarketers, only to be frustrated by state law jurisdictional limits. These jurisdictional limits make it difficult to prosecute or obtain relief from fraudulent telemarketers who locate their operations outside the states in which their victims are located or move frequently to avoid detection and prosecution under state law. In addition, although VISA and MasterCard are working closely with federal and state law enforcement agencies to ensure that the maximum possible resources are devoted to addressing telemarketing fraud, fraudulent telemarketing schemes are too numerous and too widespread to be controlled by the enforcement agencies alone, given their priorities and resources.

S. 2494 and S. 1441

S. 2494 would, among other things, require the Commission to promulgate rules concerning telemarketing fraud and would provide a private right of action under which consumers, MasterCard, VISA, financial institutions and other victims of telemarketing fraud may bring lawsuits against fraudulent telemarketers. In addition, S. 2494 would permit state attorneys general to sue fraudulent telemarketers in federal court.

The Consumer Fraud Prevention Act, S. 1441, would, among other things, require the Commission to promulgate rules concerning telemarketing fraud and would authorize the Commission to appoint state attorneys general to assist the Commission in enforcing its telemarketing rules. S. 1441 would not create a private right of action.

Scope Of The Bills

Issues relating to the scope of federal telemarketing fraud legislation are, in many respects, the most important and difficult issues associated with the bills. We believe that it is critical, on the one hand, to limit the scope of the bill as narrowly as possible so as not to unduly interfere with legitimate telemarketers and other merchants while, on the other hand, not to provide "loopholes" through which sophisticated fraudulent telemarketers could escape the reach of the legislation. In this regard, VISA and MasterCard believe that it is important to stress that the purpose of this legislation is to stop fraudulent telemarketers. Legitimate telemarketers and other merchants should be excluded from the scope of the legislation, so as not to unnecessarily regulate legitimate telemarketers, who have not engaged in telemarketing fraud.

MasterCard and VISA believe that the definition of the term "telemarketing" in S. 2494 which, in part, defines the scope of the coverage of the legislation is more appropriate than the definition of that term contained in S. 1441, although some further refinement may be appropriate. Specifically, we believe that the following elements of the definition of telemarketing in S. 2494 represent appropriate limitations to the scope of this legislation: (1) the requirement in the definition of telemarketing in S. 2494 that the telemarketing be part of a "plan, program or campaign"; (2) the requirement in the definition of telemarketing in S. 2494 that the use of the telephone be to "induce purchases of goods or services"; (3)

the requirement in the definition of telemarketing in S. 2494 that the use of the telephone be "significant"; and (4) the exclusion from the definition of telemarketing in S. 2494 of "other use of a telephone in connection with business or personal transactions".

We oppose, however, the exclusion in S. 2494 of intrastate telephone calls from the definition of telemarketing. Although we recognize the ability of the states generally to address intrastate, as opposed to interstate, telemarketing fraud, we nevertheless believe that the exclusion of intrastate telemarketing will potentially provide unintended loopholes for sophisticated fraudulent telemarketers. For example, a fraudulent telemarketer could establish operations in one state, call victims located only in that state, and prior to state enforcement, move to another state. By moving from state to state and telephoning victims only in the state in which the fraudulent telemarketer is temporarily located, the fraudulent telemarketer could avoid state prosecution and the provisions of S. 2494, including the private right of action and state attorney general enforcement provided for in S. 2494. Similarly, a fraudulent telemarketer could avoid S. 2494 by establishing a separate subsidiary in each state, and limiting each subsidiary to calling victims in the state in which the subsidiary is located.

VISA and MasterCard strongly support Section 9(c) of S. 2494, which appears to limit the scope of the bill to the scope of the Federal Trade Commission Act ("FTC Act"). Accordingly, S. 2494 would appear not to apply to banks, savings associations and federal credit unions and the bill, as discussed below, should be amended to clarify such exclusion. Such a limitation is consistent with the decision of Congress to limit the scope of the Commission's authority under the FTC Act. Given the enforcement power provided the Commission under S. 2494, we believe that such a limitation is equally appropriate in this case.

Section 9(c) raises a peculiar issue with respect to depository institutions. Although banks, savings associations and federal credit unions are excepted from the FTC Act, the FTC Act requires the federal bank regulatory agencies to promulgate "substantially similar" regulations to those promulgated by the Commission under the FTC Act. MasterCard and VISA recommend that S. 2494, be amended to provide that the federal bank regulatory agencies are not required to promulgate substantially similar rules to those promulgated by the Commission under S. 2494, because S. 2494 is not part of the FTC Act and because, as discussed below, such rules are not necessary in view of the pervasive regulation to which depository institutions are subject.

VISA and MasterCard also recommend that S. 2494 be amended to exempt from its scope affiliates and subsidiaries of depository institutions. Depository institutions are exempt from the FTC Act because they are subject to extensive "cradle to grave" regulation under applicable federal and state banking laws. Subsidiaries and affiliates of depository institutions are subject to this same pervasive regulatory structure, pursuant to which any inappropriate telemarketing activities would be adequately addressed. (We would be pleased to provide to the Subcommittee a paper detailing the regulatory structure to which depository institutions and their subsidiaries and affiliates currently are subject.) Subjecting depository institution subsidiaries and affiliates to S. 2494 would unnecessarily impose on such entities duplicate and potentially inconsistent federal regulation. Moreover, there has been no indication in Congress' two-year investigation of telemarketing fraud that depository institutions or their affiliates or subsidiaries are part of the telemarketing fraud problem; indeed, they are frequently the victims.

For these reasons, MasterCard and VISA would recommend that depository institutions affiliates and subsidiaries -- as well as the depository institutions themselves -- be excluded from the bill. Without such an exemption, VISA and MasterCard would not be able to support the bill. MasterCard and VISA also would not object to exempting from S. 2494 other regulated industries, which could demonstrate that their applicable regulatory structures effectively address their telemarketing activities.

Finally, VISA and MasterCard believe additional exemptions to S. 2494 may be warranted, for example, where there has been an in-person meeting between the seller and the customer prior to consummation of the transaction, the seller is responding to an unsolicited request or inquiry from the customer, or the customer is solicited by means of a bona fide catalog. There has been no evidence that these types of transactions are part of the telemarketing fraud problem, and subjecting these transactions to S. 2494 would unnecessarily regulate legitimate merchants.

Commission Rules

MasterCard and VISA believe that Commission rules concerning telemarketing fraud would provide valuable assistance in identifying impermissible telemarketing activities. Given the problem that S. 2494 and S. 1441 are designed to address -- telemarketing fraud -- the Commission's rules required under these bills should be limited to fraudulent telemarketing. Many of the telemarketing rules the Commission is required to consider under S. 2494 and S. 1441 do not directly address telemarketing fraud. For example, rules regarding shipping times, buyer cooling off periods, the hours of the day when telemarketing calls may be made and the equipment that telemarketers must use do not necessarily relate to telemarketing fraud.

Accordingly, we recommend that S. 2494 and S. 1441 be amended to explicitly prohibit telemarketing fraud, and to require the Commission to adopt rules limited to telemarketing fraud and to prevent persons from engaging in such telemarketing fraud. The specifics of these rules should be left to the Commission, as the expert federal agency in this area, to develop and amend over time as telemarketing fraud evolves.

Private Right Of Action

VISA and MasterCard believe that the type of private right of action contained in S. 2494 is an essential element of any effective federal response to telemarketing fraud. Such a private right of action would permit those who are in the best position to first detect telemarketing fraud -- the victims -- to act quickly to stop fraudulent operations as soon as they are discovered. Because S. 2494 would permit such actions to be brought in an appropriate federal court, victims could obtain appropriate relief, regardless of where in the United States the fraudulent telemarketers are located or have moved. As a result, MasterCard, VISA, financial institutions and other victims who are currently stymied by the limitations of state laws could more effectively utilize their own resources to assist in the fight against telemarketing fraud.

VISA and MasterCard recognize, however, that any new remedies to address telemarketing fraud must contain appropriate safeguards to ensure that legitimate telemarketers and other legitimate merchants are not inappropriately affected. For example, S. 2494 requires that a plaintiff must suffer $50,000 in damages to bring a private cause of action against a fraudulent telemarketer. MasterCard and VISA support this $50,000 jurisdictional threshold, which is consistent with federal jurisdictional requirements generally and would ensure that the federal courts are not unduly burdened with small cases. In this regard, however, VISA and MasterCard recommend that the bill be amended to provide that the amount in controversy for an action brought by an organization comprised of financial institution members is the aggregate of the amount in controversy claimed by the individual members of the organization.

MasterCard and VISA also recommend that S. 2494 be clarified to provide the federal courts with exclusive jurisdiction over all private causes of action brought under S. 2494. This appears to be the intent of S. 2494, and would encourage consistent interpretation and application of S. 2494 throughout the nation. The bill does not, and should not, restrict any right a person may have to pursue in state or federal court remedies under any other statute or common law.

State Attorneys General

VISA and MasterCard also believe that the state attorneys general should play a significant role in the solution to the telemarketing fraud problem. MasterCard and VISA have worked closely with the state attorneys general and have found them to be responsive in pursuing fraudulent telemarketers under state laws. As discussed earlier in this testimony, VISA and MasterCard are quite sensitive to the current jurisdictional restrictions impeding the effectiveness of the state attorneys general with respect to telemarketing fraud enforcement. Thus, MasterCard and VISA believe that federal legislation to address telemarketing fraud should contemplate a significant enforcement role for the state attorneys general, which is carefully structured given federal and state law considerations. In this regard, we believe that the independent role provided the state attorneys general under S. 2494 is more appropriate than the more limited Commission "deputization" procedure provided for the attorneys general under S. 1441.

Effectiveness Of Private Cause Of Action And State Attorneys General Enforcement

If lawsuits are to be effective in addressing telemarketing fraud, it is critical that the plaintiffs in these lawsuits be permitted access to the courts as quickly as possible upon discovery of telemarketing fraud. Given the speed with which fraudulent telemarketers change names or locations, or transfer assets beyond the jurisdiction of the court, it is essential that parties initiating legal action, at a minimum, be permitted to obtain preliminary injunctive relief as quickly as possible at least to preserve the status quo. In addition, our experience indicates that each day fraudulent telemarketing operations are permitted to continue often results in significant additional losses for the innocent victims of the fraudulent telemarketing operator.

Accordingly, VISA and MasterCard strongly support the provisions of S. 2494, which require notice to the Commission contemporaneous with, rather than prior to, the initiation of a civil action under the bill. We believe that these provisions provide for appropriate coordination with the Commission, without unduly impairing the effectiveness of private causes of action and state attorneys general lawsuits to address telemarketing fraud.

Additional Technical Recommendations

In addition to our recommendations for amendments to S. 2494 described generally in our testimony, we have a number of additional technical suggestions which we believe are necessary to refine and clarify certain provisions of S. 2494. For example, we believe that Section 9(c) of S. 2494 should be amended to clarify that all of the provisions of S. 2494 do not apply to entities exempt from Commission jurisdiction under Section 5(a)(2) of the FTC Act.

We would be pleased to work further with the staff of the Subcommittee in this regard to make this telemarketing fraud legislation as effective as possible in addressing this important national problem. We also would be happy to direct our Washington counsel, Morrison & Foerster, to work with the Subcommittee staff in this regard.

Senator **Bryan**. Thank you very much, Mr. Collier.

Congressman Santini is going to be batting clean up this morning on this panel.

Welcome to the panel.

STATEMENT OF JAMES D. SANTINI, WASHINGTON, DC REPRESENTATIVE OF THE NATIONAL TOUR ASSOCIATION

Mr. **Santini**. It is a privilege, given the distinguished panel you have assembled here, Mr. Chairman.

I am James D. Santini, Washington representative of the National Tour Association. Today, I am appearing before this committee on behalf of President George Guenther and the 5,000 members of the National Tour Association, NTA.

My testimony is in support of S. 2494. In 1988, and again in 1989, NTA testified in support of comparable legislation before the House Subcommittee on Transportation and Hazardous Materials.

Before I present our views, I would like to provide you with background information of the National Tour Association. NTA has been in existence for 38 years. Our membership includes more than 500 tour operators in the business of developing, packaging and selling group tours to destinations in the United States, Canada and throughout the world.

Also included in NTA's membership are destination marketing organizations, who represent local, regional, state and provincial travel promotion offices, and our 2,000 suppliers, which represent attractions, hotels, motels, restaurants, bus companies, airlines, receptive operators and many others.

The focal point of our association is our 525 tour company members. NTA and our tour company members place a very high priority on professionalism and quality service. The operator members must abide by a strict NTA code of ethics that assures proper business activity between the individual members for the ultimate good of the traveling public. We are extremely proud of the professional reputation that the association membership has throughout the country.

The reputation of the National Tour Association has been reinforced by some specific consumer protection initiatives. In order to be admitted to the association, an NTA tour operator member must maintain at least a $1 million policy in errors and omissions on a professional liability insurance and must have been in business and operating tours for at least two years.

Also, NTA provides all tour operator members with a $100,000 consumer protection program, which in the event of a member's declaration of bankruptcy, repays consumer deposits up to an aggregate amount of $100,000. NTA has placed $1 million of its equity in a fund, in a reserve account, in order to make this program a reality.

In support of the consumer protection plan, NTA has put into place a consumer awareness and information campaign. The campaign has included a series of press releases and public appearances throughout the United States by volunteer leaders. Through these efforts, the consumer protection plan has gained national recognition in the media. Publicity on the plan and the response by consumers is quickly causing the NTA logo to be recognized as the "mark of quality."

As I mentioned earlier, marketing is a key element in our tour company members' business. One marketing approach used by many of our members is that of telemarketing. Our members strive to educate and train their staffs to carry out this approach in a highly professional, ethical manner. As a result of this, we are very sensitive to the issue of fraudulent telemarketing, and commend you, Mr. Chairman, and your committee for taking the lead in drafting legislation to address this important issue.

One predicate for the NTA support of S. 2494 is the recognition that a few notorious travel scam operators can spoil many other apples in our tour operator barrel.

A fraudulent, boiler room rip-off operator gives a black eye to thousands of hard working tour operators and travel agents. The travel scam exploiters also create the real possibility that states will adopt various regulatory and punitive statutes that may inadvertently trap the honest and diligent operator in a records-keeping and fee-paying net. The end result is burdening or harassing the innocent and responsible operator while the unscrupulous promoter ignores the regulations because he has no intention of complying with the law in the first place.

In NTA's judgment, S. 2494 strikes a reasoned and responsible legislative balance in responding to the challenge of the Nation's illicit telemarketers. NTA hopes that this legislative expansion of the Federal Trade Commission's authority will dissuade each state from enacting a myriad of registration and communication constraints that will substantially burden the reputable operator engaged in packaging and marketing travel services throughout the country.

Certainly Sections 3(d) (1) and (2) contemplate possible state legislation. But the FTC general rules and guidelines will certainly establish a uniform tone and guidepost for any subsequent state legislative or regulatory action without preempting that state action.

More effective legal weapons are needed in the battle against telemarketing exploiters and criminals. S. 2494 will enhance both the Federal Government's and the states attorneys general's legal weapons.

Thank you, Mr. Chairman.

Senator BRYAN. Congressman Santini, we appreciate your testimony on behalf of the National Tour Association.

I have a few questions I would like to direct to the panel. Ms. King, let me begin with you, if I may.

Mr. Barton makes what, at least on the face of it, appears to be a reasonable argument for exceptions from the legislation, and he cites two examples. One, he says that if it is an inbound call, which I understand to be a call that was unsolicited by the telemarketer, but a customer makes a call into a place of business and says I would like to order this item or purchase this manner. And the other example he cites is where there has been a pre-existing business relationship between the customer and the telemarketer.

And he argues, at least on the face of it, that those are a couple of categories that ought to be excepted, that that is not the unsolicited call that arrives at your home or your place of business when your thoughts are many miles away from buying a particular service or a product.

Does he make a good argument for the exception in your view? And if not, why not?

Ms. KING. I think, number one, that I cannot really see any reason to accept any kind of call because we would run into definitional problems. Telemarketing fraud is so closely related to other kinds of fraud, to include credit card and mail fraud, that defining the exact nature of the pre-existing relationship and so forth, might be very difficult.

I recognize the legitimacy and, in some cases, almost personal relationship between some businesses and some of their clients. But in those cases, I would think, the good reputation would preclude the requirement that they be excluded from the rule. In other words, I cannot see what the problem is. And I think that would be the general conclusion of NACAA.

Senator BRYAN. Mr. Barton, let me give you the chance to respond and let us put a little different spin on the question. You represent legitimate telemarketers, and I have acknowledged, as has Senator McCain, that it is not our intent to tar all of you with the same brush. There are clearly responsible people. There are billions and billions of dollars of commercial commerce each year that are legitimately undertaken by a telephone solicitation.

Your members all wear the proverbial white hat. They are going to abide by the rules. They are going to live by the standard of ethics that you have outlined. Why would they be concerned about being included, even if they were making the inbound call and there was a pre-existing relationship, because presumably they are the good guys and they are not going to victimize people by the kind of practices that we are trying to get at in this legislation?

Mr. BARTON. I think they would be concerned, Senator, largely because we are charting unknown waters here if this bill passes the way it is.

They are concerned over inconsistent, let us say, interpretations of fraud laws that they may have no knowledge of or no understanding of. It may be in some cases irrational, I tend to agree with you.

I think that very few, if any, of our members would have anything to worry about this bill—with the approaches we have overall in this bill, but they are really very concerned that they might be tarred with an inconsistent interpretation or something which they are not aware of. And they would like to have a recognition of the fact that in fact the kinds of activities they are doing are legitimate and to be exempted from them, to the extent that we are explaining here, for a very good reason, if we can get the right definition, as Ms. King said, so they would not have to be concerned.

That might be a vague answer, and I could probably give you a written response better, but I can tell you that even the perfect L.L. Beans of the world are concerned about 50 state attorneys general having 50 different interpretations of Federal fraud laws. And they would like, if they have a preexisting relationship with a customer, to be exempted from this. And I tend to agree with them.

The argument can cut both ways. If in fact we have nothing to be concerned about, we have nothing to be concerned about adopting our recommendation.

Senator BRYAN. I take it your members do not live by a daily standard, have you hugged your attorney general today?

Mr. BARTON. We love our attorneys general.

Senator BRYAN. There is still a concern that these formidable men and women are on the prowl. I understand what you are saying, Mr. Barton.

Let me focus on this cooling off period, which frankly is of interest to me. You were in the room when I commented that in years past, in the Nevada legislature, serving there as a member 20 years ago, we passed for the first time the door-to-door solicitation cooling off period.

Given that there might be some bona fide exceptions, and you talked about stocks and bonds and insurance and perishable items, I do not want to concede that point, but for the purpose of discussion, let us assume that there are some things that maybe ought to be taken out of a cooling off period.

Philosophically, should not the customer who is solicited without an invitation or inquiry by himself or herself at least have the right within a reasonable time period to say, gee, I was not thinking when I got that call, and I had something on the stove or I was out mowing the yard when I was approached about this handy-dandy gadget that might trim or edge or reduce the burdens in the kitchen to a fraction of the time I spend there? Now I have thought about this thing and I really do not need that at all.

What is wrong with that, in terms of policy, in terms of good business relationships between people who are longstanding?

Mr. BARTON. Nothing. In fact, I would agree with you that as a standard, general policy of business, you ought to provide the customer a cooling off period. And this is a very strong part of our own guidelines to businesses.

The only point I was making is that it is different to have a guideline than an absolute regulation requiring a three-day—our guidelines call for a three-day cooling off period—than an absolute regulation that you have to have a cooling off period. Because there may be some, as you pointed out and as I pointed out, sometimes when the cooling off period is not appropriate or even desirable from the viewpoint of the consumer.

So as I said, our approach would be your approach, to let us have the Federal Trade Commission look into it and develop a regulation that can recognize some of those possible exceptions.

Senator BRYAN. And I take it, Mr. Barton, that if this legislation is processed, that you would work with the Federal Trade Commission in promulgating such a regulation, recognizing that there may have to be some exceptions and some different variations? I can appreciate that that might occur. But I am pleased to hear that at least you recognize that the customer ought to have a right under those circumstances to reconsider his or her judgment.

Mr. BARTON. We have a long history of working very positively with the Federal Trade Commission on regulations. The 30-day rule, or what is known as the mail order rule, in fact was largely a matter of joint cooperation between this association and others and the Federal Trade Commission. We think it has worked very well.

We are working with the Federal Trade Commission now as the only intervenor, I think, in the case in which we are calling for expansion of the mail order rule to telemarketing. So we feel that we may not always agree, but that we can have a good relationship with them, because they trust us to describe the legitimate parts of the business.

Senator BRYAN. Mr. Barton, you have the reservation about the authority of the attorneys general to proceed under any rules that are promulgated under the Federal fraud cause of action which is created by this bill. And you indicate you favor the deputized approach.

Would you not concede, and Attorney General McKay cited a corollary—it was not exactly in point because he was referring to being deputized by the U.S. Attorney's Office, and admittedly that is a bit different—but recognizing that the Federal Trade Commission, even with the attitude that has been expressed and acknowledged by Attorney General McKay and others—that Chairman Steiger is working constructively with the attorneys general, and she recognizes that they have a positive and a very helpful role to play, that just the sheer mechanics of a Federal bureaucracy which is large and frankly is remote from many areas in the country, by definition, that because there is a need to act and to act very quickly because of the migratory nature of these businesses, that in point of fact, the deputized concept just represents a delay that we cannot afford in terms of ferreting out the very people that your legitimate telemarketing organization wants to see out of business because they create a problem for you?

You all tend to get lumped into the same barrel of bad apples, to use the metaphor that the Congressman made reference to. Would it not be to your best interest to have quick and vigorous action taken?

Mr. BARTON. I have to preface this with my standard disclaimer, that I am not an attorney. I do not know whether that is good or bad for me.

Senator BRYAN. Well, that may give you additional credibility here in the Congress.

Mr. BARTON. And my attorney is sitting right behind, and he is probably shooting daggers at me right now. So I do not know in-depth the technical details you are talking about. I understand what you are talking about, so my next answer to the last question is yes, even if we are going to use the deputized approach. Because we are not opposed to attorneys general having a very strong role in this, it has to be done faster than apparently what was described.

We agree, you need to turn around within 24 or 48 hours in many cases to do that. We would like to see, and this is where I get my attorney into it, some way that we could work out a way for that process to happen very quickly, but still giving the Federal Trade Commission a strong role in at least enforcing some sort of consistency of interpretation of fraud statutes.

Senator BRYAN. Mr. Barton, if you will permit me to make an observation. One of the remarkable things of the past decade is that heretofore the conventional wisdom of the generations of people in the business community is, please, do not let the Federal Government get involved in this sort of thing, we can handle this at the state and local level. That is a refrain that I have heard for nearly two decades as a member of state, legislative and later an executive relationship.

The failure of the Federal Government to act responsibly at the Federal level in the past decade encouraged almost by necessity—there being a vacuum having been created—the kind of aggressive action that now ironically gives at least some of your members some pause. Not to be critical of the concern. I think perhaps it is overstated, and as you know, I come down on a different side of that equation. But had we had this aggressive enforcement action at the Federal level in the 1980s, I would respectfully submit that your testimony might be considerably different today.

Mr. BARTON. As a former teacher of political science, I have realized and been amused by the ironies of the situation.

Senator BRYAN. I am amazed by it, but you are not the only one, and I do not mean to cite you.

Mr. BARTON. There are historical swings, starting from 1787, along these lines, as you know. This is a personal statement and not from a DMA viewpoint, because I have not submitted this.

I agree with you 100 percent. I think that in a business such as we represent, which is direct marketing, which, by its very nature, implies that we are much more involved in interstate commerce that intrastate commerce—I mean our mail goes all over the country, and the telemarketing goes all over the country—that we have an interest as an industry for overall Federal consistent regulation that we can know and understand and have it consistently applied in Texas or Massachusetts or Maine, perhaps more so than a lot of others.

So we are pretty strong supporters of Federal regulation, and I have to admit personally that we would not be here if in fact some of these laws had been enforced much more vigorously on the Federal level.

Senator BRYAN. Mr. Barton, I appreciate your candor.

Mr. Collier, why should we exempt the depository institutions? Could you encapsulate that argument? I know you tried to make the case in your written testimony, and it must have been very late last night. I must say that I was not following it as I should, and I am refreshed this morning, so let me give you a chance to make that here if you would, please.

Mr. **COLLIER**. Well, we do feel that there are sufficient regulations on the books now for those various agencies. And we would be pleased to submit a graph indicating all this to the subcommittee if you so desire.

Senator **BRYAN**. Would you do that, to give you a chance to—we will hold the hearing record open on the specifically what regulations in your view makes it unnecessary for you all to be included?

I have to tell you it is a jump ball right now, as far as I am concerned. I really do not know enough about the regulations to which you alluded, but maybe you will be able to make the argument that will persuade a majority of this subcommittee, if indeed there is appetite to process this legislation, as I hope there will be.

Mr. **COLLIER**. I will comply with that.

Senator **BRYAN**. How about the cooling off period? Mr. Barton indicates philosophically he agrees with it. Where do you all come down on that argument?

Mr. **COLLIER**. As for the cooling off period, I do not believe it really affects the telemarketing fraud. From our own experience, the telemarketer, as soon as that phone is hung up, has already submitted the draft to charge the cardholder's account. And the cooling off period certainly would not apply at all in this case.

Senator **BRYAN**. Well, let us assume that you are correct, that the telemarketer is, by definition, under those circumstances, the telefraud I believe is the word that Mr. Barton prefers to use, okay, by definition, we have got an act of telefraud that is about to occur, and maybe you are correct. But let us talk about the philosophy in a little broader sense.

Someone, again, is solicited in his home or her home, or place of business, and makes one of these decisions on the spur of the moment, why should not that customer, even assuming a legitimate telemarketing solicitation, not tainted by fraud, why should not that person have the right, within a reasonable period of time, to say, look, that was a terrible decision I made last night over the telephone, I thought about it the next morning and I really do not need that? Or at least I ought to go out and independently shop.

Mr. **COLLIER**. Visa and MasterCard both support the FTC proposal to do just that.

Senator **BRYAN**. All right. I appreciate that, Mr. Collier.

Congressman Santini, tell us a little bit about the telemarketing fraud that you have encountered in the tour business. You made reference to it in your testimony. How widespread do you find it to be, the bad operators that are not part of the association that you represent?

Mr. **SANTINI**. It seems to be more rampant in the decade of the 1980s than it is perhaps today, as a consequence perhaps of the States of Illinois, California and Florida, instituting an aggressive prosecutorial action.

And as Attorney General McKay alluded to today, certainly the aggressive actions in the State of Nevada has helped to deter some of that boiler room phone set up, where 40 phones randomly call in targeted districts, usually where seniors reside, promising exotic trips to attractive ports of call in the Caribbean, on the Danube and Hawaii, asking only for permission to use their credit card number in order to close this once-in-a-lifetime deal because it only remains open for the next 24 hours.

And it has caused considerable consternation within the profession of the tour operator, in particular. Because if you have one scam operator in one community, say, a suburb of Chicago, Illinois, the headlines that that scam operator generates as a consequence of their multimillion-dollar exploitations, creates a market dampening impact on the entire tour operator business in that area. And particularly when calling to an area in which the scam operator had targeted and victimized.

And NTA has really launched an aggressive public relations campaign to try and persuade the perspective traveller to identify with the NTA logo as their guarantee of security when purchasing the product. But, do not know that the association has enough money to get that information to every prospective victim of a travel scam operation.

Senator BRYAN. Congressman, does your organization have any problem with the abilities of the attorneys general to act if this went into effect, the proposal that we have in our bill, by just simply giving notice, as opposed to the deputizing concept that Mr. Barton would prefer, and that the Federal Trade Commission would prefer?

And I do not recall whether you were here when the testimony was offered, but the preference clearly expressed by the Commission is, look, we would like to be able to deputize the attorneys general, as opposed to letting them file and proceed in Federal court under the Federal Cause of Action or under any rule that we might promulgate as a result of the hearings that we undertake?

Mr. SANTINI. That specific issue had not been laid on the NTA board of director's table. But if I can speak privately and individually, borrowing on Mr. Barton's scenario so he does not get in trouble with his boss.

Mr. BARTON. I might still.

Mr. SANTINI. I do not oppose the notice provision, as a matter of practical efficacy. The travel scam operator moves in and out as quickly as any of the telemarketing or telefraud operators that you have heard testified to here this morning. And if you have a substantial length of time between the initiation of the legal process, be it civil or criminal, and the conclusion of that process, a telescam operator can be out of town in less than 24 hours. That is the practical reality. And if there is some other practical way to deal with it, I would be receptive to hearing it, but I do not know what it is.

Senator BRYAN. I appreciate your candor and your disclaimer is in the record for your employers.

Does the fact that we suggest the consideration of a cooling off period, a two- or three-day period of time, or whatever it might be, does that give your organization any heartburn?

Mr. SANTINI. I think you might consider, Mr. Chairman, the Nevada exception. That is, anyone solicited and agreeing to make a trip to the State of Nevada is bound by that commitment, irrespective of any subsequent change of plans.

Senator **Bryan**. I cannot imagine that they would ever want to cancel such an intriguing trip. I cannot conceive of that.

Mr. **Santini**. It is inconceivable to me, too, Mr. Chairman. But absent that one exception, NTA does not oppose the cooling off period.

Senator **Bryan**. Well, we appreciate that.

You have all been very candid and forthright, and we appreciate very much your testimony. The record reflects the points of view.

Let me just indicate to you that because some of the members of the subcommittee could not join us today because of a conflict and may have some questions, we are going to hold the record on this hearing open for a while. You may receive some questions by mail from our staff or from the staffs of the subcommittee members. We would like to ask you to respond, if you would, in a timely fashion so that we might have those comments if there are any.

No further business appearing today before this subcommittee, this hearing stands adjourned.

[Whereupon, at 11:33, the hearing was adjourned.]

ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

OFFICE OF THE CHAIRMAN

March 16, 1990

The Honorable John McCain
United States Senate
Washington, D.C. 20510-6125

Dear Senator McCain:

Thank you for your letter of December 6, 1989, requesting the Federal Trade Commission's views on S. 1441, the Consumer Fraud Prevention Act of 1989. We believe the bill would be of substantial assistance to the Commission in its fight against consumer fraud, and commend you for your efforts. The views set forth in this letter are those of the entire Commission.

Below, we first describe some of the law enforcement problems we encounter in combatting consumer fraud, and then offer comments on the specifics of S. 1441.

As you observed in introducing the bill,[1] consumer fraud comes in many guises. Each year, consumers lose billions of dollars due to the fraudulent sale of goods and services. Many of these frauds present enormous difficulties for law enforcers.

An example is telemarketing fraud, specifically addressed in S. 1441. The classic example is the fly-by-night telephone "boilerroom" that peddles millions of dollars of worthless goods over the telephone and then disappears, reappearing elsewhere under a different name. If made aware of a government investigation, the individuals operating these scams often will close shop and flee, hiding assets and destroying incriminating records. Thus, effective law enforcement requires construction of the case without alerting the targets. This is a formidable task, given the difficulty of finding victims and former employees, establishing oral representations, and locating consumer monies without the targets being informed of the inquiry.

These investigations and subsequent lawsuits also can be complex and resource-intensive. For example, it may take sophisticated expert testimony to prove that the seller's investments or other offerings are not as represented. To make a case for consumer redress, the Commission also must present convincing evidence of a broad pattern of misrepresentations. This can be difficult where oral representations are the heart of the fraud. Finally, the Commission often must send teams of lawyers to the target's home jurisdiction to file suit and assist in the seizure of records and assets. Litigation can be protracted, sometimes extending to bankruptcy court where the Commission is seeking consumer redress and competing with other creditors for the company's assets.

---

[1] 135 Cong. Rec. S9142-45 (daily ed. July 31, 1989) (statement of Sen. McCain).

The Commission is proud of its efforts in combatting consumer fraud. The Commission has brought some 48 cases in federal court since 1983 against fraudulent telemarketers alone. The target companies had sales of over $740 million, involving a wide variety of scams -- the fraudulent sale of gemstones, oil leases, government lottery application services, oil and gas drilling ventures, silver and gold ore processing contracts, rare coins, vacation packages, fake art, business equipment and supplies, and employment services.

A cooperative federal-state law enforcement approach using both civil and criminal weapons can go far towards controlling telemarketing fraud. In general, we believe that legislative efforts in this area should be consistent with the following two principles.

First, it is important to facilitate the use of criminal enforcement tools in combatting consumer fraud. These frauds, for the most part, are a highly lucrative criminal activity. Many perpetrators have criminal records and no qualms about bilking consumers, including widows on pensions. Many scam artists become millionaires through this activity. Although civil law enforcement can substantially hinder their activities, scam operators fear criminal prosecution above all. We believe that increased criminal law enforcement is indispensable to controlling consumer fraud, and encourage criminal law enforcement by appropriate federal and state authorities whenever we find evidence of criminal fraud in our cases.

Second, civil law enforcement should focus principally on stopping the most egregious practices -- the deceptive tactics that induce purchasers to buy goods and services that, if not worthless, are worth far less than represented. We recognize that other problems may be of concern to consumers, such as phone calls late at night, abusive computerized calls, and so forth. However, it is the fraudulent sale of goods and services that has cost consumers billions of dollars. At a time of budget constraints, law enforcement resources should remain targeted on attacking these core violations.

We believe that S. 1441 is true to these principles and would substantially assist the Commission and the states in combatting consumer fraud. Below, we comment on the specific provisions in the bill.

Venue and Compulsory Process

The Commission ordinarily attacks consumer fraud using its permanent injunction authority under section 13(b) of the FTC Act, 15 U.S.C. § 53(b). The most efficient route is to bring all charges against all potential defendants in one lawsuit. However, section 13(b) now requires that suit be brought in the district where each defendant "resides or transacts business." This creates a potential problem where some targets, though participants in the fraud, have transacted much of their business outside the judicial district where suit is brought. There have been cases where staff, confronted with venue problems, have felt it necessary to abandon meritorious claims against such participants.

This problem will grow in importance as the Commission increases its enforcement efforts against suppliers of fraudulent instrumentalities and other aiders-and-abettors of boilerroom fraud. Frequently, the more complex schemes involve a network of firms and individuals spread over many states. Getting at the root of such frauds often will involve suing the principal aider-and-abettor in its home jurisdiction, and trying to join as defendants as many of the participating boilerrooms as possible, wherever located.

Section 4(a)(1) of Senate Bill 1441 would remedy these venue problems by making it clear that the Commission may sue all such defendants in one district when a federal court finds that the ends of justice so require. This would be a welcome amendment to our statute. We also would recommend the addition of language to allow the court to serve its process on the defendant "wherever it may be found."[2] Without such a provision, service of summons

---

[2] Specifically, we recommend the following revisions to the amendment to section 13 already contained in the bill:

> Sec. 4. (a) Venue and Process. -- (1) Subsections (a) and (b) of section 13 of the Federal Trade Commission Act (15 U.S.C. 53) are each amended by adding at the end thereof the following: "All process of any court to which application may be made as provided in this subsection may be served upon the defendant wherever it may be found.

(continued...)

outside the state in which the court sits depends upon the vagaries of state long-arm statute requirements, which in particular instances may not be broad enough to reach out-of-state defendants. Congress has provided for such extraterritorial service of process in similar contexts. See, e.g., 15 U.S.C. § 22 (Clayton Act); 18 U.S.C. § 1965 (RICO); 15 U.S.C. § 77v(a) (SEC).

Section 4(a)(2) of S. 1441 would further amend the FTC Act to address, for the first time, the manner in which the Commission may serve process in section 13 actions. Currently, the Commission serves process pursuant to the provisions of Rule 4 of the Federal Rules of Civil Procedure. Essentially, Rule 4 gives the Commission the service-of-process options set out in the Rule itself, or those provided by relevant state law. We have no objection to the substitute service-of-process provisions in S. 1441, but note that the current scheme has proved satisfactory. We would recommend one change to section 4(a)(2), however. The phrase "any process of the Commission" should be changed to "process of the court," to reflect the fact that section 13(b) cases are brought in federal court.

Finally, we strongly support section 4(b) of S. 1441, which would amend the FTC Act to enable the Commission to require the production of physical evidence pursuant to civil investigative demands. Currently, section 20 of the FTC Act only permits the Commission to require the production of documents or testimony. The above provision in the bill would enhance our ability to investigate telemarketing scams. For example, where a company

---

[2] (...continued)
Whenever it appears to the court that the interests of justice require that any other person, partnership, or corporation should be a party in such suit, the court may cause such person, partnership, or corporation to be summoned without regard to whether they reside or transact business in the district in which the suit is brought, and to that end process may be served ~~in any district~~ wherever the person, partnership, or corporation may be found.

The Commission would also favor changing the word "shall" in the venue language in Sections 13(a) and (b) [i.e., the final sentences in these provisions that recite that "Any such suit shall be brought in the district in which such person, partnership, or corporation resides or transacts business."] to "may" so as to make clear that the venue provisions do not foreclose application of the general venue provisions found in 28 U.S.C. § 1391. The permissive "may" is typically used in other special venue provisions, e.g., section 12 of the Clayton Act, 15 U.S.C. §22.

allegedly is misrepresenting the value of rare coins or lithographs, the Commission would be in a better position to obtain samples of these items from suppliers or other third parties and have them appraised by experts.[3]

Right to Financial Privacy Act

The Commission ordinarily tries to locate potential defendants' assets before suit is filed. The Commission then requests that the court grant ex parte asset freeze orders that immediately can be served on all relevant financial institutions before the defendants can hide their assets. Obviously, this pre-complaint search for assets must be conducted without alerting the target individuals. The Right to Financial Privacy Act,[4] however, makes this difficult with respect to the assets held by financial institutions for individuals and certain small partnerships. Currently, the Act requires that such customers of financial institutions be notified of federal agency inquiries, with certain exceptions. These exceptions are not specifically tailored to address situations where investigative targets are likely to dissipate assets obtained through fraud.

Section 4(d) of S. 1441 would remedy this problem by adding a new exemption applicable to the routine fraud case. Specifically, federal agencies could delay notice where a federal district court finds, inter alia, that there is reason to believe that notice will result in "dissipation, removal, or destruction of assets that are subject to forfeiture, seizure, redress, or restitution under any law of the United States by reason of having been obtained in violation of law."

---

[3] Section 4(c) of the bill would have the beneficial effect of granting the Commission access to mail covers, which, under current postal regulations are only made available to agencies in connection with criminal investigations. The language of section 4(c) is an improvement over that of the predecessor bill, S. 2326, in making clear that the Commission would have the same power to obtain mail covers as "law enforcement agencies investigating the commission or attempted commission of a crime." The corresponding referent in S. 2326 was "other law enforcement agencies," which arguably would have included some civil law enforcement agencies that do not have access to mail covers and, unlike the Commission, do not even investigate criminal fraud-type activities.

[4] 12 U.S.C. § 3401 et seq.

We welcome this provision, and suggest only one modification to make the process less cumbersome. If section 4(d) of S. 1441 were to be adopted without change, the Right to Financial Privacy Act, arguably, still would require the Commission to file an ex parte, sealed complaint in the home district of every financial institution from which it seeks information.[5] Often, individuals and small partnerships running consumer frauds maintain numerous financial accounts spread over the country. In such circumstances, the search for individual and partnership assets would remain a difficult task. One solution would be to further amend the Right to Financial Privacy Act to permit the Commission and other federal agencies to file applications with "any district court of the United States within the jurisdiction of which such inquiry is carried on." This is the language in section 9 of the FTC Act that describes the courts to which the Commission may apply to enforce subpoenas.

This approach would retain judicial protection of the privacy rights of financial institution customers, while greatly reducing the Commission's time and travel burden. Headquarters staff often could obtain judicial approval in the U.S. District Court for the District of Columbia, and Commission regional staff often could obtain court approvals in their home cities.

Assistance of State Attorneys General

The Commission and state law enforcement authorities have enjoyed a close working relationship in a host of fraud investigations and cases. The states and the Commission routinely share information, refer cases to one another, give one another logistical assistance, and divide law enforcement responsibility in cases of overlapping jurisdiction. S. 1441 would promote even closer cooperation by authorizing the Commission to appoint state attorneys general to assist the Commission in enforcing Commission rules.

We not only support the state-appointment provision in S. 1441, but also recommend that it be broadened in two respects. First, we recommend that the state-appointment authority be granted not only for the enforcement of Commission rules, but also for permanent injunction cases under section 13(b) of the FTC Act against telemarketers engaged in fraudulent practices. Although state participation in enforcing Commission rules is desirable, rule enforcement is not the weapon of choice with respect to the target of the bill -- consumer fraud. Typically, the essence of the fraud is the misrepresentation of the value of goods and services sold, a practice ordinarily attacked through section 13(b) lawsuits.[6]

---

[5] Under 12 U.S.C. § 3409(a), the Government must obtain "an order of an appropriate court" granting the requested delay of notice to the customer and prohibiting the bank from disclosing the government inquiry to the customer. (emphasis supplied) Although "appropriate court" is not defined in the statute, this term could be read as requiring the Government to file the application in the federal judicial district within which the financial institution is located.

Second, we urge that the Commission be authorized to appoint not only state attorneys general, but also other officials granted civil or criminal law enforcement authority under state law. One such law enforcement authority is the Florida Comptroller's Office, which brings enforcement actions against a wide range of consumer frauds, including the types of investment frauds investigated by the Commission.[7] The Commission also works closely with a number of district attorney's offices in attacking consumer frauds. We see no reason to limit appointments to attorneys general offices, especially if the appointment authority is extended to telemarketing fraud actions brought under section 13(b) of the FTC Act.[8]

As the Commission stated in its comments on S. 2326, introduced by you in the last Congress, we believe this approach of appointing state attorneys general is preferable to direct enforcement by the states of the FTC Act or Commission rules.[9] The appointments approach, while promoting federal-state cooperation, would ensure consistent application of the FTC Act. Furthermore, the appointments approach would pose less risk of being challenged on constitutional grounds. The Department of Justice, commenting on the direct-state-enforcement provisions in two other telemarketing bills last year, expressed the view that these provisions would run afoul of the Appointments Clause.[10]

---

[6] Specifically, we recommend that section 4(e)(1) be amended as follows: "When the public interest so requires and the Commission has reason to believe that any person, partnership, or corporation subject to its jurisdiction is violating any Commission rule or is engaged in telemarketing fraud, the Commission may appoint State attorneys general, or any other officials granted civil or criminal law enforcement authority under state law, to assist Commission attorneys in enforcing such rules or in bringing permanent injunction cases under section 13(b) of the FTC Act against such telemarketers."

[7] See e.g., Fla, Stat. Ann. §§ 20.12 and §§ 517.01 et seq. (giving the Florida Comptroller's Office the power to intercept various investment frauds).

[8] We note that the fifteen-day deadline for Commission response to requests for appointment sometimes will be impractical in complex matters. However, this should be little problem if, as we expect, the appointments scheme encourages the states to consult with Commission staff early in the investigative process.

Mail Order Rule

Section 5 of S. 1441 would require the Commission to amend the Mail Order Rule, 16 C.F.R. § 435, to apply to sales made over the telephone. Section 5 would further require that the Commission, as part of this rulemaking, consider a number of other provisions, including a three-day cooling-off provision applicable to telemarketing sales.

We question the need for section 5 of the bill on several grounds. First, the Commission already is formally considering the one provision that would be mandatory in section 5(a) of the bill -- the extension of the Mail Order Rule to cover telephone sales. On November 28, 1989, the Commission published a Notice of Proposed Rulemaking to consider whether such an amendment of the Rule is desirable. 54 Fed. Reg. 49,060 _et seq_. (November 28, 1989). Public hearings on the rulemaking are now scheduled for March 28, 1990. We believe that this rulemaking will provide the most comprehensive basis on which to decide whether the benefits of extending the Mail Order Rule to telephone sales outweigh the costs.

---

[9] Statement of the Federal Trade Commission Before the Consumer Subcommittee, Committee on Commerce, Science and Transportation, U.S. Senate, September 13, 1988, at 9-10, 17-18.

[10] Letter from Thomas M. Boyd, Acting Assistant Attorney General, Office of Legal Policy, U.S. Department of Justice, to the Hon. John McCain, United States Senate, September 27, 1988 (commenting on S. 2213 and H.R. 4101, both entitled the Telemarketing Fraud Prevention Act of 1988.) The issue is whether states, in enforcing Commission rules, would be acting as "Officers of the United States" when enforcing federal laws that vindicate public rights. Only persons appointed pursuant to the Appointments Clause may exercise such functions. _See_ _Buckley_ v. _Valeo_, 424 U.S. 1 (1975).

We also note that the proposed extension of the Mail Order Rule to telemarketing would only affect delayed delivery of goods sold by telephone. This is not the essence of most telemarketing frauds. In such cases, the evil usually is not delayed shipment, but rather the deceptive sale of the goods and services. Similarly, the three-day cooling-off provision contemplated in section 5(b)(2) of S. 1441 would not affect the vast majority of fraudulent telemarketing transactions, because the consumer typically is unaware that he or she has been defrauded until long after the initial transaction. In sum, amendments to the Mail Order Rule may be a matter best left to normal Commission review and rulemaking processes.[11]

Finally, section 5 of S. 1441 also requires that the final rule amendments be adopted not more than 270 days after the passage of the bill. This deadline may prove impossible to meet, depending on the date of passage of the bill. The Commission, as required under the FTC Act, is conducting the Mail Order Rule proceeding under the complex rulemaking procedures mandated in The Magnuson-Moss Warranty - Federal Trade Commission Improvement Act, 15 U.S.C. § 2301. The bill, by introducing new issues, may further lengthen this proceeding.

One solution would be to authorize the Commission to conduct whatever rulemaking is required by section 5 of the bill pursuant to the notice-and-comment procedures set out in section 553 of the Administrative Procedures Act, 5 U.S.C. § 553. In that event, a further authorization also would be desirable -- authorization for the Commission to seek civil penalties for violation of this section 553 rule.[12] Currently, the Commission only has the authority to seek civil penalties for violations of rules regulating unfair or deceptive acts or practices that are promulgated under authority of the FTC Act. The foregoing amendment would make clear that the Commission could seek civil penalties for violations of the rule contemplated in S. 1441, even though the bill, rather than the FTC Act, would have been the impetus for a number of the rule's provisions.

---

[11] We recommend the following minor revision to section 5(d) of the bill: "For purposes of this section, a financial institution or other participant in a payment system used to pay for products or services offered or sold through telemarketing, including the credit or payment authorization aspect of such payment system, is not, solely by virtue of such participation, a telemarketer nor a person, partnership, or corporation which acts in concert with, or on behalf of, a telemarketer." This revision, while consistent with the section's intent, would clarify that sellers of goods otherwise subject to the Rule could not evade its requirements by also offering or participating in credit arrangements with the consumer.

Life Care Home Study

Section 6 of S. 1441 would require the Commission to conduct a study of unfair and deceptive acts or practices in the life care nursing home industry and, within two years, to report its findings to Congress. The Commission would be required to indicate in the report if it intends to commence a rulemaking to address abuses in the industry and the reason for its decision. In the Commission's March 1988 hearing on issues affecting the elderly, you and others voiced important concerns about the financial problems many elderly have experienced in the life care home industry. We share these concerns and support this provision of S. 1441.

Long-Term Health Care Insurance Study

We similarly welcome the provision in section 7 of S. 1441, which directs the Commission to conduct a study concerning unfair or deceptive acts or practices in the sale of long-term health care policies to the elderly. The Bureau of Consumer Protection, in its report to Congress in September 1988 on Medigap insurance, described the major issues and suggested that the marketing of long-term health care insurance might be a fertile area for further study.[13] Currently, the Commission is prohibited from studying insurance absent a request to do so by either the Committee on Commerce, Science, and Transportation of the Senate, or the Committee on Interstate and Foreign Commerce of the House of Representatives, 15 U.S.C. § 46(h). Section 7 of S. 1441 in effect would give the Commission one-time authority to conduct this study pursuant to a Congressional request.

---

[12] An example is the language in the "Petroleum Marketing Practices Act," 15 U.S.C. § 2801 et seq. The Act required, inter alia, that the Commission promulgate the Octane Labeling Rule under the notice-and-comment procedures of 5 U.S.C. § 553. The Act went on to say that "[f]or purposes of the Federal Trade Commission Act (including any remedy or penalty applicable to any violation thereof) such a violation shall be treated as a violation of a rule under such Act respecting unfair or deceptive acts or practices . . . ."

We offer only one caveat. Section 7(a)(2) of S. 1441 requires that the Commission address the relationship of premiums for long-term health care policies to expected claims paid under such policies. In May 1987, the General Accounting Office noted that long-term health insurance is a new product, and that there is a relative dearth of insurance loss experience. Notably, the pay-out periods for such insurance sometimes can last two decades. In sum, loss data on this insurance product may be difficult or impossible to obtain. We simply note that, because of these uncertainties, we are not in a position to judge whether the deadline of one year for conducting the study will be sufficient.

Proposed Additions

Below, we suggest two additional amendments to the FTC Act that would assist the Commission in its fight against consumer fraud.

First, we recommend that S. 1441 amend section 16 of the FTC Act to explicitly authorize the Commission, after consultation with the Justice Department, to bring criminal contempt actions for violations of orders obtained in section 13(b) cases. This would be the same consultation procedure by which the Commission now brings civil penalty and other federal court actions as to which it does not now have exclusive litigating authority. As in civil penalty actions, the Justice Department would retain the right of first refusal to bring such actions, to be exercised within forty-five days of notification by the Commission.[14]

---

[13] Federal Trade Commission, Bureau of Consumer Protection, Marketing of Medigap, Specified Disease and Hospital Indemnity Insurance to the Elderly: Report to the Committee on Energy and Commerce, U.S. House of Representatives (September 1988).

The proposed amendment would be an important complement to our enforcement powers under section 13(b) of the FTC Act. As stated before, scam operators are adept at resurfacing with new frauds under new names, and fear criminal prosecution more than civil suits. Staff has encountered instances where scam operators have hidden assets or re-opened new fraudulent businesses in violation of existing court orders. With the above authority, the Commission would be in a position to act quickly against violators of orders, the Justice Department retaining the option to take action itself.

---

[14] Specifically, we recommend that section 16 of the FTC Act be revised to read as follows:

> Sec. 16. (a)(1) Except as otherwise provided in paragraph (2) or (3), if --
>
> (A) before commencing, defending, or intervening in, any ~~civil~~ federal court action involving this Act (including an action to collect a civil penalty) which the Commission, or the Attorney General on behalf of the Commission, is authorized to commence, defend or intervene in, the Commission gives written notification and undertakes to consult with the Attorney General with respect to such action: and
>
> (B) the Attorney General fails within 45 days after receipt of such notification to commence, defend, or intervene in, such action;
>
> the Commission may commence, defend, or intervene in, and supervise the litigation of, such action and any appeal of such action in its own name by any of its attorneys designated by it for such purpose. The Commission may bring a criminal contempt action for violations of orders obtained in cases brought under section 13(b) of the Act in the same manner as civil penalty and other federal court actions to which section 16(a) applies. Such cases may be initiated by the Commission on its own complaint, or pursuant to its acceptance of an appointment by a court to assist it in enforcing such orders pursuant to Rule 42(b) of the Federal Rules of Criminal Procedure.

One avenue for pursuing criminal contempt actions is to refer such cases to the Justice Department. However, there are inevitable delays in obtaining action in such instances, given the Department's heavy criminal caseload and differing priorities. Some have argued that the Commission is not authorized to bring its own criminal contempt cases in such instances. Although the Ninth Circuit has rejected such arguments,[15] explicit statutory authorization would eliminate the delay engendered by these arguments and ensure that the Commission, after consultation with the Justice Department, could move quickly against order violators. In so doing, the Commission would not be urging interpretations of criminal statutes enforced by the Justice Department, but rather would be asking courts only to enforce the very orders that the Commission had obtained by its own attorneys under section 13(b) of the FTC Act.

Second, we recommend that S. 1441 amend section 5(m)(1)(B) of the FTC Act to extend the Commission's existing civil penalty authority. Currently, that section authorizes the Commission to bring civil penalty actions in federal court against persons who have actual knowledge that their conduct violates the FTC Act. A pre-condition to such suits is a prior Commission determination in a cease and desist order proceeding that the specific practice is unlawful. Such a Commission order, or synopsis thereof, can be sent to others in the industry who are engaged in the same practice, putting them on notice that they may be charged with civil penalties if they continue this practice.

The Commission cannot exercise this civil penalty authority if a federal court, rather than the Commission, has made the determination that a specific practice violates the FTC Act. We recommend that section 5(m)(1)(B) be amended to permit civil penalty suits where federal courts, as well as the Commission, have made such determinations.[16] This added civil penalty

---

[15] In F.T.C. v. American National Cellular, Inc., et al. and Godfree, 868 F.2d 315 (9th Cir. 1989), defendants claimed that the Commission lacked authority to accept court appointment to conduct a criminal contempt case under Fed. R. Crim. Proc. 42(b). The court upheld this authority, there having been "some involvement" of the Justice Department in the process.

[16] Specifically, we recommend that section 5(m)(1)(B) be amended as follows: "If the Commission determines in a proceeding under subsection (b) or a court determines in a case brought under section 13(b) of this Act that any act or practice is unfair or deceptive, and the Commission issues a final cease

(continued...)

authority would be an important supplement to the existing injunctive and redress remedies in section 13(b) cases. Besides its general deterrent effect, civil penalty authority would provide the Commission with a monetary remedy where redress to consumers or other equitable remedies are impractical.

Thank you once again for the opportunity to provide our views on S. 1441. The Commission stands ready to assist you in your further consideration of the bill.

By direction of the Commission.

Janet D. Steiger
Chairman

---

[16] (...continued) and desist order or a court enters a final order with respect to such act or practice, then the Commission may commence a civil action to obtain a civil penalty in a district court of the United States against any person, partnership, or corporation which engages in such act or practice . . .." In this connection, subsections 5(m)(1)(B)(1) and 5(m)(1)(C)(2) also would require amendment to refer to court orders as well as Commission cease and desist orders.

STEPHEN BARRETT, M.D.
CONSUMER ADVOCATE
P.O. BOX 1747
ALLENTOWN, PA 18105
215-437-1795

April 30, 1990

The Honorable Richard Bryan
United States Senate
Washington, DC 20510

Dear Senator Bryan:

Sherman Joyce has asked me to suggest ways your committee could act against health frauds and quackery. I have several suggestions.

Three federal agencies have responsibility in this area. The Postal Service has jurisdiction over products sold by mail. It has a vigorous program but is hampered by a weak law. The FTC has jurisdiction over the advertising of nonprescription products and services. It has a powerful law but insufficient manpower. The FDA has jurisdiction over the labeling of products marketed with therapeutic claims. It has a powerful law, but a pitiful enforcement record. Overall, there is little to deter people from violating existing laws.

Almost all health products advertised for sale by mail through newspapers and magazines are bogus. When the Postal Service detects a scam, it can use an administrative procedure to block money and orders from reaching the perpetrators. But a persistent perpetrator can still take orders through a toll-free number and deliver via United Parcel Service. Even if a scam is stopped, the perpetrators may still make an enormous profit between the time the ad is placed and the time the Postal Service intervenes. Thus, no matter how many schemes are stopped, there is still an incentive to try new ones. Correction of this situation can be accomplished by four simple measures:

- Pass a law enabling the Postal Service to issue or negotiate civil penalties (possibly as high as three times the gross sales of the product) as part of its consent agreements or false representation orders. This would enable the Postal Service to make mail fraud much less profitable. A share of the penalties could be given to the complainant and/or nonprofit groups involved in fighting health frauds.

- Pass a law stating that if the Postal Service obtains an order blocking use of the U.S. mail, it could also block delivery through private carriers, such as United Parcel Service.

- Pass a law that would make it practical for the Postal Service to initiate *criminal* prosecution in cases where health products are involved. To obtain a conviction under current mail fraud laws, intent to deceive must be proven. This is difficult to do if a perpetrator professes a belief in his product. Federal drug laws have no such requirement. Under these laws, it is a crime to market a drug that is unapproved or misbranded. It is not necessary to prove that the marketer had an intent to deceive.

- Pass a law giving the Postal Service authority to issue civil investigative demands. This would would speed up investigations by enabling postal inspectors to gather information from the seller that would be difficult or impossible to obtain from other sources.

The Federal Trade Commission has a very powerful law but has been able to average only five or six cases a year involving health frauds. The problem seems to be lack of manpower. The solution is simple. State attorneys general handle dozens of similar cases each year involving health frauds, but these actions affect only the state in which the action is brought.

- Pass a law empowering state attorneys general to enter federal court so that any court order they obtain is binding nationwide. Senator Metzenbaum introduced such a bill last session.

When the FDA detects illegal marketing, it can issue a warning letter, initiate a seizure, seek an injunction, or initiate criminal prosecution. Criminal prosecution would have the greatest deterrent effect, but it is rarely used. Civil action, which carries no financial penalty, stops some schemes, but does not usually prevent them from being profitable.

- Pass a law enabling the FDA to issue or negotiate civil penalties in the same manner as the Federal Trade Commission. A share of the penalties could be given to the complainant and/or nonprofit groups involved in fighting health frauds.

It would also help if all three of these agencies were forced to be more accountable. As far as I know, none of them has ever revealed meaningful statistics about the number of law violations they have detected and what percentage of them they have acted against. Statistics of this type would enable legislators and the public to see the scope of the problem and what might be done about it.

- Pass a law requiring the FDA, Postal Service and FTC to make meaningful data available on what the agencies are doing about health frauds and quackery. This can be done by maintaining a list of prosecutions, both in progress and completed, that is accessible year-round through the agency's public information office and is published at least once a year in a report to Congress. The report should include tabulations of the number of health-related complaints received, the number judged valid, and the number subjected to regulatory action. The agencies should also be required to recommend improvements in the law that might enable them to work more effectively.

Sincerely yours,

Stephen Barrett

Stephen Barrett, M.D.

ASTA

American Society of Travel Agents
P.O. Box 23992, Washington, DC 20026-3992
1101 King Street, Alexandria, VA 22314 USA
(703) 739-2782 • Telex 440203 • FAX (703) 684-8319

May 18, 1990

The Honorable Richard H. Bryan
Chairman
Subcommittee on Consumer
Committee on Commerce, Science and
 Transportation
United States Senate
Washington, D. C. 20510

Dear Senator Bryan:

On behalf of the American Society of Travel Agents (ASTA), I am writing to express support for your legislation, S. 2494, the Telemarketing Fraud and Abuse Prevention Act.

ASTA is the world's largest trade association of professional travel agents, with 13,000 travel agency members throughout the United States, and a total worldwide membership of agents and industry suppliers exceeding 22,000.

ASTA's members are primarily small business owners and their employees. Among ASTA's purposes are the promotion and advancement of the interests of travel agents and the safeguarding of the traveling public against fraud, misrepresentation and other unethical practices.

We are critically aware of the extent of telemarketing fraud with respect to travel scams. In 1987, ASTA's Consumer Affairs department held a conference in Washington, D.C. entitled, "What is a Travel Scam." Its primary purpose was to identify the different types of travel scams and educate the consumer on evaluating travel offers. Two conferences were held in 1988 in Chicago and Los Angeles on "Solutions for Travel Scams." As a result ASTA produced a consumer brochure, Avoiding Travel Problems and co-produced, with the Federal Trade Commission, a video news release on travel scams.

It was evident from conference participants, including several Attorneys General, that telemarketing fraud in the form of travel scams has been extremely difficult to enforce. Oftentimes, since the overhead of these perpetrators consists merely of a telephone and post office box, these criminals can rapidly move their operations across state lines to avoid enforcement of the present law.

ASTA has discussed this matter with Representative Luken, the sponsor of H.R. 1354, the Telemarketing Fraud Prevention Act, who has also received letters from concerned constituents. On March 16, 1989 a hearing was held before the House Commerce Subcommittee on Transportation and Hazardous Materials on telemarketing fraud prevention at which ASTA gave testimony.

Since the current system offers no solution to the problem, we look forward to the FTC taking a more active role in regulation of telemarketing practices, as provisions in your legislation would stipulate. Also, crucial to the enforcement of these practices, is an across the board application of these rules. We feel that exempting any industry from regulation would be counterproductive to the goals of the legislation. It is essential to provide the Attorneys General with additional powers to cross state lines and prevent perpetrators from evading justice.

The clearinghouse operation which you envision in Section 8 of your bill is a positive step. This will provide an easier way for states and individuals to monitor activities and get information on telemarketing fraud activities in other parts of the country. It will assist in the collective efforts to combat abuse and protect consumers from becoming victims of travel scams.

ASTA has always found telemarketing fraud to be a difficult problem to control through legislation. However, we feel that your bill meets the needs of honest telemarketers, while providing necessary protection for consumers. We appreciate your efforts and the efforts of the Committee and stand ready to assist you in increasing co-sponsorship, building support and, ultimately, securing passage of this important legislation.

Very truly yours,

Voit Gilmore

Voit Gilmore, CTC
President and Chief
Executive Officer

UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

OFFICE OF
THE COMMISSIONER

May 25, 1990

The Honorable Richard H. Bryan
Chairman, Consumer Subcommittee
Committee on Commerce, Science
and Transportation
United States Senate
Washington, D.C. 20510

Dear Chairman Bryan:

As you know, I joined in the testimony of May 2, 1990 on telemarketing legislation presented by Federal Trade Commission ("FTC" or "Commission") Chairman Janet Steiger on behalf of the entire Commission. Like my colleagues, I think that telemarketing fraud is a matter of serious concern and accordingly welcome legislation that would make it easier to prosecute fraudulent telemarketers. Indeed, since the Commission currently deserves credit for pursuing these cases vigorously within the limits of existing budgetary restrictions and legal authority, constructive legislation could provide significant new momentum for the fight against telemarketing fraud.

I am writing separately now simply to provide my perspective on one aspect of the testimony from May 2nd. In essence, I cannot embrace all of the Commission discussion concerning the state enforcement provisions of S. 2494 and S. 1441. In particular, I think that the appointments approach outlined in S. 1441 is not necessarily preferable to the separate cause of action approach set forth in S. 2494.

The separate cause of action approach set out in S. 2494 and the appointments approach delineated in S. 1441 both would provide welcome enhancements for state enforcement authority without greatly imperiling FTC authority. S. 2494 would permit state attorneys general to enforce the Commission trade regulation rule to be promulgated governing telemarketing practices as well as Commission telemarketing fraud orders, and to bring parens patriae actions under a new telemarketing fraud cause of action. S. 1441 would permit the Commission to appoint state attorneys general to assist in trade regulation rule enforcement. The Commission has suggested that this authority be expanded to permit the FTC to appoint state officials to assist in permanent injunction actions brought under Section 13(b) of the FTC Act against fraudulent telemarketers. I believe either approach would provide important opportunities for cooperative federal-state enforcement efforts against telemarketing fraud.

Of course, the possibility of inconsistent application of the FTC Act is a serious concern that both bills admirably address. In this regard, it seems to me that S. 2494 actually runs less risk of inconsistent application of the FTC Act than does the expanded appointment approach recommended by the Commission for S. 1441. Indeed, in February 1988 the Commission told Chairman Luken that any new telemarketing legislation "would be accomplished most appropriately in a separate statute."[1]

As stated then by the Commission, creating a separate cause of action would diminish the risk of introducing any element of ambiguity into the Commission's basic enabling legislation, while maintaining the Commission's ability to respond flexibly under the FTC Act.[2] Similarly, the likelihood of inconsistency created by state enforcement of the trade regulation rule proposed by the legislation would be slight since Commission rules set out with specificity required courses of conduct and do not require interpretation of the FTC Act's prohibition against unfair or deceptive acts or practices. Finally, enforcement of Commission orders would raise minimal risk of inconsistency. This risk would be minimal because the issue raised in such a proceeding would be focused on whether the defendant complied with the specific prohibitions or affirmative obligations of the Commission order, and the Commission previously would have expressed its views regarding deception or unfairness questions.

The appointments approach set out in S. 1441 similarly runs a low risk of inconsistent enforcement by requiring Commission review of every case before a state can participate in it and restricting the appointments authority to rule enforcement. The appointments approach, however, will be of limited value to cooperative federal-state enforcement activities unless it is expanded in the manner suggested by the Commission to include permanent injunction actions brought under Section 13(b) of the FTC Act against fraudulent telemarketers. But, this expansion would lead to direct enforcement of the FTC Act and increase the risk of inconsistency -- unless the legislation is intended to relegate states to a ministerial role in the prosecution of such cases.

---

[1] Letter from Daniel Oliver to The Honorable Thomas A. Luken, Chairman, Subcommittee on Transportation, Tourism, and Hazardous Materials, Committee on Commerce, United States House of Representatives at 2 (February 11, 1988).

[2] Id.

One other aspect of S. 1441 worth mentioning is that while Commission review of all proposed state cases would reduce the risk of inconsistency, it also necessarily would lead to delay. Experience has shown that the likelihood of obtaining meaningful consumer redress is directly correlated with the speed with which the Commission staff secures preliminary relief in court. Thus, any delay is troubling. Indeed, fear of the kind of delay that could be created by an appointments approach underlies the Commission's request for expanded authority to bring criminal contempt actions for violations of Section 13(b) orders.[3]

S. 1441, of course, could be crafted to minimize "review delay" by requiring Commission action on a state's request for appointment within a very short time. This, however, could relegate Commission review to a pro forma exercise. Because state actions under S. 1441 would result in direct enforcement of the FTC Act, pro forma review would increase the risk of inconsistent application of the Commission's jurisdictional basis of authority.

In sum, both the direct cause of action proposed by S. 2494 and the appointments provision set out in S. 1441 merit commendation as important methods of increasing enforcement actions against fraudulent telemarketers. However, at this time, the case has not been made that the appointments approach has greater potential for increasing state-federal cooperation than does the direct cause of action approach.[4]

Thank you for this opportunity to present my additional comments for the record. Please let me know if I may be of further assistance.

Sincerely yours,

Andy Strenio

Andrew J. Strenio, Jr.
Commissioner

---

[3] See Commission testimony at 16.

[4] The Commission testimony notes that legislation creating a new federal cause of action permitting states to prosecute telemarketing fraud might be challenged as unconstitutional under the Appointments Clause. Lacking a thorough briefing on this possibility, I express no views on its merits. I note, however, that the Clayton Act expressly authorizes states to bring parens patriae actions on behalf of their citizens. To my knowledge, no such action has ever been dismissed based upon an argument that this provision violates the Appointments Clause.

GENERAL COUNSEL
Law Department
Washington, DC 20260-1100

May 15, 1990

Honorable Richard H. Bryan
Chairman, Subcommittee on Consumer
Committee on Commerce, Science,
and Transportation
United States Senate
Washington, DC 20510-6132

Dear Mr. Chairman:

The Postal Service would appreciate inclusion of the following comments in the record of the Subcommittee's hearings on proposed legislation dealing with telemarketing fraud, including the bills S. 2494 and S. 1441.

The Postal Service generally supports the purposes of these bills. We strongly oppose one provision, section 4(c) of S. 1441, which would require the Postal Service to amend its mail cover regulations to permit the Federal Trade Commission to obtain access to mail covers in its civil administration of section 5 of the Federal Trade Commission Act (FTCA) (15 U.S.C. § 45) "to the same extent and in the same manner as law enforcement agencies investigating the commission or attempted commission of a crime."

Information on the covers of undelivered mail matter about particular postal customers which the Postal Service obtains through the performance of its official postal functions is generally held by the Postal Service as private and confidential information not disclosed to anyone other than the sender or addressee. Domestic Mail Manual (DMM) 115.5, incorporated by reference, 39 C.F.R. § 111, proposed 42 Fed. Reg. 18,754-18,758 (1977), adopted without objection as to § 115.5, 43 Fed. Reg. 14,308-14,315 (1978). One narrow exception is for mail cover reports made pursuant to the Postal Service's mail cover regulations, DMM 115.5(b); 39 C.F.R. § 233.3. Mail cover reports are investigative reports made by the Postal Service to an investigating government agency of information which the Postal Service collects from the covers of undelivered mail matter not addressed to the investigating agency, such as the name and address of the addressee or sender or both, the class of mail service, and information in any postmark or postage meter marks.

Postal mail cover regulations currently restrict eligibility to apply for and obtain mail cover information to those federal, state, and local agencies which are authorized to investigate the commission of a "crime", which these regulations further define as any act whose commission or attempted commission is punishable by imprisonment for a term exceeding one year. 39 C.F.R. § 233.3(c)(1), (3), (4), (d)(2)(ii), (e)(1)(ii). The three grounds presently allowed by the regulations for the issuance of a mail cover order (an order allowing the collection and reporting of such information to an investigative agency) are to protect the national security, to locate a fugitive, and to obtain information regarding the commission or attempted commission of a crime. 39 C.F.R. § 233.3(c)(1), (d)(2)(ii), and (e)(1)(ii). Protecting the national security is restrictively defined so as to encompass only assistance for counter-terrorism investigations directed toward the thwarting of discrete, serious, and hostile foreign threats. 39 C.F.R. § 233.3(c)(5).

FTC investigations in furtherance of FTCA § 5 are investigations of "unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce * * * ." 15 U.S.C. § 45(a). The Commission's authority to prevent such unlawful commercial activities is essentially the regulatory authority to issue orders and regulations after conducting administrative proceedings. 15 U.S.C. § 45(a)(2), (b). FTC orders are subject to federal judicial review. 15 U.S.C. § 45(d), (h)-(j). Any person who violates an FTC order or rule is subject to a "civil penalty" which may be recovered from the violator through a "civil action" in court. 15 U.S.C. § 45(l), (m).

FTC investigations in furtherance of FTCA § 5 are not criminal investigations. They are not eligible for mail cover support under current postal mail cover regulations.

The privacy of information about postal customers on the covers of mail matter has long been recognized by U.S. postal regulations. Such information, being necessarily exposed to the view of postal employees, is not considered as private as the contents of a mail article which is sealed against postal inspection, which is given by U.S. constitutional and statutory law the same privacy as the sender would enjoy as if he or she had retained his papers or objects in his or her home. 1/

1/ Ex parte Jackson, 96 U.S. 727, 732-733, 735 (1878) (unanimous opinion); United States v. Van Leeuwen, 397 U.S. (continued...)

The confidentiality of mail cover information is nonetheless generally protected by the postal system, in recognition that its primary mission is to serve its customers rather than investigate them or publicly expose their private affairs, and in deference to long-standing customer expectations that the postal system will generally respect the privacy of such information. Heretofore, the only regulatory exceptions allowed for disclosing mail cover information to government investigators has been to enable them to protect the national security, locate a fugitive, and to obtain evidence of the commission or attempted commission of a crime. 44 Fed. Reg. 24,113 (1979).

Strict protection of the confidentiality of mail cover information while it is in the postal system also serves to protect the public interest in protecting the mail transmission operations of the postal system from undue interference and the postal system's ability to serve the public at least cost. Recording information from the covers of mail matter which is not required to be recorded in order to deliver the mail necessarily imposes operational costs and the potential for delay of mail. An extremely limited number of mail cover orders for the surveillance of an extremely limited categories of mail matter can of course be accommodated annually without any significant adverse operational effect. But if mail coverage were conducted on a wide scale, the costs of such coverage could become significant. In addition, service itself could be impeded, as the burden of recording and reporting information about mail compelled the diversion of postal personnel and resources from mail transmission and delivery functions to mail cover recording and reporting functions.

Present mail cover regulations create only extremely limited exceptions for mail coverage. Only a few thousand mail cover orders result each year, a number which is minuscule in relation to the postal system's hundreds of millions of customers and the more than 160 billion pieces of mail annually sent and received. Present grounds for allowing mail coverage, which are to protect the national security, locate a fugitive, or obtain evidence of a crime or attempted crime, serve in practice to restrict mail cover requests to extremely unusual situations.

These three grounds work in practice to limit the scope of mail coverage requested or needed. To locate a fugitive, it is normally necessary only to watch the mail addressed to the person, or few persons, who are very close to the fugitive.

1/ (...continued)
249, 250-251 (1970) (unanimous opinion); 18 U.S.C. § 1702; 39 U.S.C. § 3623(d).

Likewise, in the case of mail covers to protect the national security (as restrictively defined by postal regulations) or to obtain evidence of a crime or criminal attempt, it is normally necessary to place under surveillance only certain types of mail addressed to a particular addressee, in criminal cases typically only for a limited period of time.

The three present grounds for mail coverage also serve to restrict how confidential mail cover information is actually used or exposed to public view. Mail cover information which is reported either to locate a fugitive or to protect the national security is normally disclosed by the postal system only to another government agency for its own internal use rather than public dissemination. Public disclosure normally does not follow. Even in criminal proceedings, where the public disclosure of mail cover information in the proceeding is a possibility, this possibility is sharply curtailed by the secrecy normally required for the success of a criminal investigation, the formal rules of evidence which are strictly applied in criminal proceedings, and the possibility in a criminal proceeding of court-imposed sanctions for prosecutorial or investigatory misconduct.

This legislative proposal unjustifiably would undermine a critical element of the Postal Service's mail cover system, which presently is working well.

The legislation would breach the present prohibition against mail coverage for civil matters, a prohibition which the Postal Service observes in denying mail coverage even to its own civil mail and program fraud investigations. The breach would, moreover, invite requests for additional exceptions, since no compelling rationale is apparent for allowing an exception for FTC civil investigations under FTCA § 5 but not other civil investigations. If FTC civil investigations are granted an exception, requests for other civil exceptions would necessarily follow. The range of federal, state, and local civil proceedings is necessarily very broad.

The practical effect on mail privacy and postal operations of an unlimited exception for FTCA § 5 proceedings could greatly exceed the nearly inconspicuous effect of the present exceptions for detecting evidence of crime, protecting national security, and locating a fugitive. FTCA § 5 investigations seek to elicit information about "unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce * * * ." Entire lines of commerce or trade can properly come under investigation. Tens, hundreds, or thousands of business firms, thousands or millions of customers, and countless business advertisements and transactions, could come within the purview of the FTC's regulatory interest under FTCA § 5. Local, regional, national and international markets can be investigated.

The copying and reporting of information on millions or even billions of pieces of mail theoretically could be requested under the legislation now proposed.

The FTC could be expected to use and disclose mail cover information in ways which could embroil the mail cover program in needless controversy. We understand, for example, that the FTC is interested, among other things, to use mail cover information to identify target businesses' customers, in order to elicit complaints or evidence against businesses under suspicion. Law enforcement agencies now authorized to request mail coverage under present regulations normally avoid systematically contacting persons whose mail privacy expectations have been invaded.

These agencies normally keep mail cover information within the government for its internal use, to develop investigative leads, to locate a fugitive, to develop protective counter-terrorism measures necessary to protect the national security, or to investigate a crime or criminal attempt. Disclosure of mail coverage may of course be made to the target of the investigation during the course of discovery, if the target should be indicted after the investigation is completed. Persons whose names and addresses turn up under mail cover surveillance, who are not themselves under suspicion, are not routinely notified now.

The possible use of mail information to develop market or like commercial information for use in the FTC's public regulatory proceedings (which are subject to judicial review) thus risks that private information concerning persons completely innocent of any wrongdoing may be routinely disclosed publicly, in civil regulatory and adjudicatory proceedings of which public records are normally kept open for public inspection for months or years, without little or no protection to the persons whose privacy has been invaded for the purpose of developing information pertinent to FTCA §5 proceedings.

Although the FTC has sought to counter such criticism by arguing that it needs legislation of this character in order to perform an implied investigative duty to investigate criminal matters which it incidentally unearths during the course of an FTCA §5 civil investigation, this argument is not compelling, in our view, as many of the Government's civil investigations may potentially disclose evidence of a crime. When the FTC, in the performance of a regulatory function, uncovers evidence of a criminal violation, it may request assistance from the Department of Justice or other agency responsible for enforcement of the criminal statute. That responsible agency would have access to request a mail cover, if justified, in accordance with current mail cover regulations.

In summary, we think that the public interest is well served by continuing to limit mail covers to their present narrow scope as necessary for criminal enforcement, to locate a fugitive, or to protect national security. The use of mail covers should not be broadened to investigations for enforcement of civil regulatory programs.

Sincerely,

Fred Eggleston

Fred Eggleston
Deputy General Counsel

Comments
on behalf of the
Association of National Advertisers, Inc.

The Association of National Advertisers, Inc. (A.N.A.) submits the following comments for the record on the important issue of telemarketing fraud.

A.N.A. is the only organization exclusively dedicated to serving the interests of companies that advertise either regionally or nationally. Its membership includes companies whose more than 2,000 subsidiaries, divisions and operating units market a variety of goods and services and collectively account for almost 80 percent of all regional and national advertising expenditures in the United States.

Background

A.N.A. generally does not focus on the telemarketing area. But the telemarketing bills pending before the Senate Consumer Subcommittee raise fundamental issues which A.N.A. believes must be addressed.

First and foremost, S. 1441 and S. 2494 raise very basic questions as to the appropriate relationship between the federal government and the states concerning the regulation of interstate commerce. In A.N.A.'s view, responsibility for regulating interstate commerce should reside predominantly with the federal government.

The telemarketing arena is particularly complex and diverse. Telemarketing fraud operations frequently impact a number of states simultaneously. A.N.A., therefore, is certain that development of a coordinated and effective regulatory policy for combating telemarketing fraud in the United States will prove virtually impossible without federeal direction.

A.N.A. agrees that telemarketing fraud is a major national concern. Consumers may lose over $1 billion annually to telemarketing con artists. Telemarketing fraud, however, is not just a consumer issue. It is also of major concern to honest businesses. Fraudulent telemarketers, by pretending to represent legitimate companies, are able to undermine the goodwill these companies have spent years developing with their customers. It is difficult to place a dollar value on how much telemarketing fraud has cost legitimate businesses. But the loss is substantial and growing. We therefore commend this Subcommittee for highlighting this critical problem and strongly support the goal of strengthening federal and state governmental efforts to eliminate telemarketing fraud.

A.N.A. appreciates the efforts of Senators Bryan and McCain to fashion narrowly tailored telemarketing fraud legislation. In our view, S. 1441 and S. 2494 collectively represent an improvement over H.R. 1354, the telemarketing legislation pending in the House of Representatives.

In determining the appropriate governmental framework to fight telemarketing fraud, it is important to emphasize that the Federal Trade Commission repeatedly has demonstrated that it is a willing policeman in the telemarketing arena. In testimony presented before this Subcommittee on May 2, 1990, the F.T.C., for example, reported:

> In recent years, the Commission has brought over fifty telemarketing fraud cases in federal court, obtaining injunctions against companies having aggregate sales of over $766 million.

A.N.A. acknowledges that the states have an important role to play in the war against telemarketing fraud. Enforcement of state civil and criminal laws is critical to curbing intrastate telemarketing fraud. We also recognize that as a result of anti-fraud efforts within their borders state officials often have important information that can be of use to federal authorities as well as to other states. The F.T.C. already has developed extensive cooperative efforts in the telemarketing area with the state attorneys general.

A.N.A. endorses the goal of achieving efficient use of federal and state resources. Unfortunately, in our view, the well-intentioned approach developed in S. 2494 is unlikely to promote an efficient allocation of federal and state resources. Instead, S. 2494 appears to grant the states primacy over the F.T.C. in regard to telemarketing fraud regulation. S. 2494 would effectively federalize the state attorneys general by granting them broad new powers to enforce state and federal telemarketing statutes in federal court. S. 2494, as drafted, also threatens to place new and potentially significant limits on the F.T.C.'s telemarketing enforcement role. Under this legislation, the F.T.C. would be saddled with broad amorphous and expensive regulatory responsibilities, including the assessment of the adequacy and effectiveness of state telemarketing fraud requirements and enforcement efforts.

In order to clarify these points, the following comments focus on those provisions of the Senate proposals of most concern to A.N.A. members. We hope that our remarks will be instrumental in assisting the Consumer Subcommittee in developing a fair and effective telemarketing fraud bill.

Section 4(a)(1) of S. 2494: This provision would authorize a state to file a civil action on behalf of its residents in federal court against any person who has engaged, is engaging or is about to engage in telemarketing which, "is a fraudulent act or practice." Unfortunately, the term "fraudulent act or practice" is not defined in S. 2494. Accordingly, this provision appears to allow the state attorneys general to bring federal suits against telemarketing schemes under their own state fraud statutes. If this is the case, then this provision provides a new and enormously broad delegation of power to the states. State fraud statutes are infinitely expandable and outside any federal control. Also, there is no reason to believe that state fraud statutes will be consistent with each other. In sum, the states, under S. 2494, will have been given broad and potentially inconsistent powers in the telemarketing area which are likely to be more extensive than the authority of the F.T.C.

Section 4(a)(1) also grants the states the power on behalf of their citizens to bring civil suits in the federal courts against any telemarketing scheme which "violates any rule, regulation or order of the Commission under this Act." Again, without federal coordination, A.N.A. believes that this broad delegation of authority to the state attorneys general is likely to lead to fragmentation of a uniform national enforcement program.

Section 4(a)(3) of S. 2494: In an apparent attempt to overcome these coordination problems, Section 4(a)(3) of S. 2494 mandates that the states provide written notice to the Commission "immediately upon commencing" a civil action in the federal courts pursuant to this Act. The Federal Trade Commission then is allowed to intervene in any such case. We do not believe, however, that allowing the F.T.C. to intervene in such cases is sufficient to assure adequate coordination between the federal and state levels. Also, Section 4(a)(3) is completely silent as to the effect, if any, of a failure by a state to provide this notification to the F.T.C. At the very least, the result of failure to carry out this requirement should not be left ambiguous; potentially, it will affect every party to the lawsuit and might serve as grounds for attacking the lawsuit itself.

Section 4(a)(7) of S. 2494: This provision would allow the F.T.C. to intervene in state civil and criminal anti-fraud cases brought under state law in state courts. In the same sense that we question an open-ended invitation to the state attorneys general to sue in federal courts under federal or state anti-telemarketing fraud statutes, we do not understand the rationale for allowing federal intervention by the F.T.C. in state courts, under state law, in regard to intrastate telemarketing issues.

Also, it is unclear to us why a state in S. 2494 is required to provide "prior written notice" of its intent to proceed in state court, but that a state is required only to provide written notice to the F.T.C. upon commencing a civil action in regard to telemarketing fraud in the federal courts. What is the rationale for giving the Commission more notice of a state's intention to enforce state law in a state court than the state is required to give when it institutes a lawsuit under federal law in a federal court?

Section 3(d) of S. 2494: This provision is a key part of S. 2494. It provides that:

> If, upon application to the Commission by an appropriate State agency, the Commission determines (pursuant to rules prescribed by the Commission) that ---
>
> (1) there is in effect a State requirement which applies to any telemarketing to which this section applies; and
>
> (2) such State requirement affords an overall level of protection to consumers which is as great as, or greater than, the protection afforded by this section; then only such State requirement shall be applicable to the extent specified in such determination for so long as the State administers and enforces effectively any such State requirement, as determined by the Commission.

While the intent of this provision appears directed to promoting coordinated and effective use of resources among the states and the F.T.C., A.N.A. believes it raises many troubling issues. If Section 3(d) is to be meaningful, it requires the allocation of substantial additional manpower and resources by the F.T.C. to carry out its mandate.

Section 3(d) requires the F.T.C. to make a series of complex, subjective and ongoing determinations regarding the comparative effectiveness of state telemarketing requirements versus federal regulation. The Commission, at the outset, would be required to evaluate whether or not the "overall level of protection" provided consumers by a state requirement is "as great as or greater than" the level of protection afforded by the F.T.C. This type of determination clearly is neither easy nor straightforward. In addition, Section 3(d) would require the F.T.C. to monitor, on an ongoing basis, the effectiveness of state activity in applying and enforcing state requirements as required by the Commission.

Rather than strengthening the F.T.C.'s own efforts with regard to combating telemarketing fraud, Section 3(d) appears to require the Commission to redirect its energies to evaluate the effectiveness and efficiency of state efforts to counteract telemarketing fraud. It is difficult to comprehend how this approach promotes the efficiency or effectiveness of the F.T.C. in the telemarketing area. Also, the required determinations under Section 3(d) often may place the F.T.C. in an antagonistic rather than cooperative posture with the states, as the F.T.C. may find it necessary to conclude that a state's regulatory programs in the telemarketing area are inadequate or less effective than are the Commission's efforts.

Furthermore, the precedents created by this legislation have broad implications. If this reallocation of enforcement responsibility to the states is warranted in the interstate telemarketing fraud area, why is a reallocation of enforcement authority, not equally appropriate in numerous other areas of interstate fraud? Is there something peculiar about the use of the telephone in interstate commerce that makes this area particularly appropriate for state regulatory action? We do not think so. The Congress should be very careful before it tilts so substantially in favor of state regulation of such a key area of interstate fraud.

Section 9(c) of S. 2494: A.N.A. believes that Section 9(c) of S. 2494 also may have unintended impacts. Specifically, while Sections 6 and 7 of S. 2494 grant the F.T.C. increased enforcement tools to combat telemarketing fraud, Section 9(c) apparently would vitiate this grant of authority. In this regard, Section 9(c) specifically provides that nothing in S. 2494 shall be construed to grant the Commission any additional authority beyond that already granted in the Federal Trade Commission Act. This result appears to be unintended, but needs to be clarified.

The Role of the F.T.C. in Telemarketing Fraud Regulation and the Issue of "Deputization"

If Congress believes more needs to be done to combat telemarketing fraud nationwide, it certainly has readily available vehicles with which to strengthen existing federal efforts. Legislation to reauthorize the F.T.C. has sat in limbo since 1982. Congress has the ability, through the F.T.C. reauthorization bill, or through other independent legislation, such as S. 2494 or S. 1441, to increase immediately the authorization levels for funding the F.T.C. Congress also can specify that a portion of this additional funding be allocated directly to telemarketing fraud suppression. Certainly, if telemarketing fraud costs consumers more than $1 billion a year, then the F.T.C.'s enforcement efforts warrant additional funding to help put an end to such abuse.

If after providing the F.T.C. with increased resources and direction concerning the telemarketing issue, Congress still finds that the states need to be given an enhanced role in the process, then the F.T.C. could be empowered, as provided in S. 1441, to "deputize" the state attorneys general. The deputization of state officials by the federal government has proven successful in other areas and permits the federal government to retain control while obtaining additional assistance from the states. The Congress can also set up procedures to assure that this "deputization" approach is both effective and timely. Certainly, this more coordinated national approach should be tried and fully tested before any thought is given to providing the states an open ended and uncoordinated delegation of responsibility in the telemarketing field as proposed in S. 2494.

F.T.C. Rulemaking under S. 2494

A.N.A. is concerned that the expedited rulemaking contemplated in S. 2494 may prove counterproductive. The goal should be to develop a rule in the complex and diverse telemarketing area that will adequately regulate fraudulent telemarketers without unduly burdening honest businesses. Compressing the rulemaking process, however, almost inevitably will assure that various affected segments of the industry will not be given adequate time to be heard fully. This is likely to engender rules which burden honest telemarketers while concurrently increasing the danger that loopholes will be created for the unscrupulous.

The rulemaking required by this legislation encompasses enormous and diverse segments of the United States business community. Also, the issues raised are not identical from area to area. It also will impact the rights of a wide range of consumers. The Senate Commerce Committee developed the Magnuson-Moss Trade Regulation Rulemaking authority to handle exactly these types of complex issues. A.N.A. does not believe that a 180 day time limit and a notice-and-comment rulemaking procedure will provide an effective framework for helping to resolve the key issues surrounding combating telemarketing fraud.

Impact on the Federal Courts

Finally, A.N.A. recommends that the Subcommittee consider carefully the burden S. 2494 will place on the federal courts. Allowing the states to enter the federal courts both under federal rules and under state fraudulent acts or practices powers is likely to place a very heavy burden on an already overworked federal judicial system. As recently as February 1989, the Chief Justice of the United States Supreme Court, William Rehnquist, in a speech before the American Bar Association warned of the overload on the federal court system. The Chief Justice stated:

> There is virtually no unused capacity in the [federal court] system as it presently exists, and the difficulties of creating substantial additional capacity counsel caution, to say the least, in attempting it. We are in a position where we must think not about creating new federal causes of action but of remitting to state courts some of the business not handled by the federal courts, and of revising the way of handling some of the business which is retained by the federal courts.

The Judicial Conference of the United States and other groups that have an overall outlook on federal court responsibilities need to be heard from before any action is taken on this legislation. Opening the federal courts to a broad range of new and uncoordinated actions in regard to federal policy, as this legislation contemplates, could result in inconsistent federal court interpretations and, unfortunately for American consumers and businesses, would place uniform national telemarketing enforcement in serious jeopardy.

Conclusion

A.N.A. believes that a carefully crafted telemarketing fraud bill will be a major step in providing protection for consumers and responsible businessmen and will help to maintain a more honest marketplace. A.N.A. stands ready to provide the Subcommittee and its staff whatever assistance it can to strengthen and refine this important legislation.

STATEMENT OF KEN EIKENBERRY, ATTORNEY GENERAL, STATE OF WASHINGTON

I appreciate this opportunity to comment on two proposed pieces of legislation which deal with the problem of telemarketing fraud, S.B. 1441 and S.B. 2494. My goal in submitting these comments is to be helpful in determining the best approach to the issues faced by the committee.

The Problem in Washington

Washington consumers, like those in many states, are prey to an ever-increasing number of fraudulent telemarketers. My Consumer Protection Division received over 14,600 complaints and inquiries involving allegations of telemarketing fraud in 1988. That number represents ten percent of all consumer complaints received by our office during that year. It is a number which is steadily increasing and shows no signs of abatement.

Who are the victims of telemarketing fraud? The statistics from my office show that businesses account for approximately 20 percent of all victims. Schemes involving the sale of office supplies, personalized pens and hats, and phony athletic calendars rank highest in our complaints from businesses. Individual consumers, who account for 80 percent of the victims, often fall prey to schemes involving so-called free prizes, vitamins, discount travel services and investment opportunities. Banks, which often absorb the consumer's loss by agreeing to cancel unauthorized charges, are also the victims of telemarketing fraud.

In 1989, Washington's state legislature passed a bill which required registration of commercial telephone solicitors, created penalties for unfair or deceptive telephone solicitation, and created a number of consumer rights and remedies. The legislation, which has been codified at RCW 19.158, requires written confirmation of telephone sales, and allows a consumer to cancel a purchase within three days of receiving a written confirmation.

Need for Interstate Enforcement in Federal District Court

The tool which Washington's legislature has given our state is a big step in the right direction. Unfortunately, it is not enough. Federal legislation which gives us the clear ability to cross state lines for enforcement is also necessary.

Fraudulent telemarketing is an interstate problem. The majority of complaints our office receives about telemarketing concern out-of-state solicitors calling Washington residents. Obtaining jurisdiction over these solicitors presents a problem.

Enforcing Washington state court judgments against them in a foreign jurisdiction presents another problem. Effectively stopping a fraudulent telemarketer who is victimizing consumers in more than one state, without duplicating the enforcement resources of several states, presents a third problem. The legislation before you today would, to a very limited extent, address these problems.

Where the FTC has established a rule, regulation or order affecting a particular practice or party, then and only then does the proposed legislation allow a state attorney general to pursue an enforcement action in federal district court. Where the fraudulent telemarketer has not violated an FTC rule, regulation or order, a state attorney general would be subject to the same uphill battle of enforcement and jurisdiction he or she is currently facing. Both S.B. 1441 and S.B. 2494 contain this limitation.

In contrast, S.B. 2213 introduced by Senator Gore on March 21, 1988, gives state attorneys general the ability to proceed against fraudulent telemarketers in federal district court regardless of the existence of any FTC rule, regulation or order. If, in fact, the goal of this legislation is to create a strong enforcement mechanism which enhances the FTC's ability to combat an interstate problem, state attorneys general should be permitted a broad means to seek effective relief. The logical forum for that relief is federal district court.

Need for FTC Rules

Both S.B. 1441 and S.B. 2494 create significant rights. I support the promulgation of FTC rules which allow for specified shipping periods, cancellation rights, restrictions on calling hours, and recordkeeping requirements. I sponsored similar legislation in Washington, and our legislators recognized a major problem area by unanimously passing the legislation. I also support the prohibition of computer-generated calling. Our state already has a statute which prohibits computer-generated calls. Both my office and our legislators received numerous complaints from constituents who bitterly resented receiving calls from a machine.

In addition to these important areas, I would encourage the committee to consider a provision granting the FTC authority to prescribe more substantive rules defining unfair, deceptive or fraudulent telephone solicitation. The creation of such rules would serve as enforcement guides for the states, and give notice to telemarketers as to what is deemed unlawful.

I welcome the opportunity to work with the FTC in enforcing its rules. Allowing the states to become involved in federal enforcement efforts is a positive step which will increase both state and federal effectiveness.

Involvement of State Attorneys General in FTC Enforcement Actions

Perhaps the biggest distinction between S.B. 1441 and S.B. 2494 is the manner in which each allows state attorneys general to institute a district court action based on an FTC rule, regulation or order. S.B. 2494 requires notice to the FTC. S.B. 1441 requires prior approval by the FTC. In order to effectuate the goal of swift enforcement, I would support the method of notice required by S.B. 2494. Prior approval creates unnecessary delay and a layer of uncertainty which will discourage state action.

Unnecessary Impingement on State's Ability to Freely Enforce

Both S.B. 1441 and S.B. 2494 takes steps to enhance the states' potential to proceed against fraudulent telemarketers. But with regard to the current draft of S.B. 2494, "what the right hand giveth the left hand taketh away." Section 4(7) of the bill seemingly requires a state taking action under its own state "antifraud" statute to give the FTC notice of such action prior to proceeding. It further gives the FTC the right to intervene, to appear, to appeal, and to appear as _amicus curiae_. Even worse, it allows the FTC to remove the action from state court to federal court.

Senate staff has explained that the intent of Section 4(7) is to allow FTC intervention and appearance only in actions under FTC rules, regulations and orders. Unfortunately, that is not clear from the current draft of the bill. As it is now written, the bill's provisions could greatly curtail a state's ability to enforce its own law. The FTC is not and should not be empowered to substitute its judgment for a state's judgment on state matters. I would strongly urge the committee to clarify the language in Section 4(7) by making it explicit that FTC involvement in state cases is limited to suits based on FTC rules, regulations and orders, and does not apply to state cases based on state laws.

Need for Private Right of Action

Finally, I would encourage the committee to expand the provision in S.B. 2494 pertaining to actions brought by private persons. Of the two bills before you, it is the only one which mentions a private action. As currently drafted, S.B. 2494 is ambiguous in its meaning and does not clearly state who may take private action. Allowing individual consumers and businesses a broad private right of action would assure a means of redress and increase enforcement activity.

MEMORANDUM

FROM: VISA U.S.A. Inc.
MasterCard International, Inc.

DATE: May 15, 1990

RE: **Federal Telemarketing Fraud Prevention Act of 1989 -- Depository Institution Exemption**

Pursuant to the request of the Consumer Subcommittee of the Senate Committee on Commerce, Science and Transportation ("Subcommittee"), this memorandum supplements the testimony of MasterCard International, Inc. ("MasterCard") and VISA U.S.A. Inc. ("VISA") before the Subcommittee during its May 2, 1990 hearing on telemarketing fraud. This memorandum expands upon the recommendation of VISA and MasterCard made at the May 2, 1990 hearing that regulated depository institutions, and their affiliates and subsidiaries, be exempted from telemarketing fraud legislation in view of the existing comprehensive statutory and regulatory scheme governing their activities, including their telemarketing activities. VISA and MasterCard hereby request that this memorandum be made a part of the record of the hearing.

MasterCard and VISA are not recommending that all entities that are subject to a federal statutory or regulatory scheme be exempted from the coverage of S. 1441 and S. 2494. Virtually all profit-making enterprises are subject to the federal income tax scheme, for example, and we are not, of course, suggesting that all such entities be exempted from S. 1441 and S. 2494. Rather, VISA and MasterCard are suggesting that because depository institutions1/ and their affiliates and subsidiaries,

---

1/ Depository institutions include any national or state bank or savings association insured by or eligible to be insured by the Federal Deposit Insurance Corporation ("FDIC") and any credit union insured by or eligible to be insured by the National Credit Union Administration ("NCUA"). See, e.g., 12 U.S.C. §§ 461(b)(1)(A) and 1815(a). This memorandum primarily addresses banks and thrifts, and their affiliates and subsidiaries. The arguments developed in this memorandum, however, apply equally to other types of depository institutions, such as credit unions.

presently are subject to a pervasive legislative and regulatory scheme under which fraudulent telemarketing currently can be effectively addressed, coverage of such entities under S. 1441 or S. 2494 would be unnecessary and result in duplication of existing regulation and unwarranted costs and expenses for these institutions.2/

Depository Institutions Are Prohibited From Engaging In Fraudulent Activities.

Although, as a general matter, regulated depository institutions and their affiliates historically have not engaged in widespread telemarketing activities, to the extent that such entities engage in telemarketing they would be subject to federal prohibitions against fraudulent activity. For example, existing federal statutes and regulations address two of the primary functions of depository institutions involving retail customers -- making loans and accepting deposits. As is discussed below, fraudulent or inappropriate telemarketing activities in these contexts would violate these federal statutes and regulations.

The Truth In Lending Act ("TILA"), 15 U.S.C. § 1601 et seq., sets forth the information that must be disclosed to consumers in connection with loans for personal, household or family purposes. For example, recent amendments to the TILA establish special disclosures that must be provided by a depository institution, or an affiliate or subsidiary thereof, that contacts a consumer by telephone to invite the consumer to open a credit card account without the need to complete an application. The TILA specifies that a depository institution conducting such telemarketing activities generally must disclose to the consumer the following information: (1) the annual percentage rate or rates applicable to extensions of credit under the credit card; (2) any annual, other periodic or membership fee imposed for the issuance or availability of the card; (3) any minimum finance charge imposed for each period during which any extension of credit that is subject to a periodic finance charge is outstanding; (4) any

---

2/ We also believe, as indicated in our written testimony which we submitted to the Subcommittee in connection with its May 2, 1990 hearing, that it may be appropriate to provide an exemption from S. 1441 and S. 2494 for other entities, such as securities firms, which also are extensively regulated. This memorandum, however, does not discuss the statutory and regulatory schemes applicable to such entities.

transaction fee imposed for the use of the credit card to purchase goods or services; (5) the grace period within which credit extended for purchases must be paid to avoid incurring a finance charge (or the fact that no such grace period is provided); and (6) the balance calculation method used to determine the outstanding balance on which a finance charge is computed. 15 U.S.C. § 1637(c)(2).

In addition, the TILA requires any commercial message in any medium, including apparently telephonic communication, that promotes directly or indirectly a credit transaction to state only the credit terms that actually are or will be arranged or offered. 12 C.F.R. §§ 226.16(a) and 226.2(a)(2).

The TILA permits consumers to bring a private cause of action against a depository institution that fails to comply with the disclosure and certain other requirements provided in that act. 15 U.S.C. § 1640. In such a lawsuit, a depository institution generally may be liable for: (1) actual damages sustained by each person as a result of the depository institution's failure to comply with the TILA; (2) in a lawsuit brought by an individual, a civil penalty of $100 to $1,000, and in a class action, the lesser of $500,000 or one percent of the net worth of the depository institution; and (3) court costs and attorneys' fees. Id. In addition, if a depository institution inaccurately discloses an annual percentage rate or finance charge, the institution may be required to pay restitution to each consumer affected by the inaccuracy. 15 U.S.C. § 1607(e).

Moreover, under the TILA, a depository institution may be fined up to $5,000 and/or imprisoned for not more than one year if it willfully and knowingly: (1) gives false or inaccurate information or fails to provide information required to be disclosed under the TILA or any regulation issued thereunder; (2) uses any chart or table prescribed by the Federal Reserve Board ("FRB") for disclosure of the annual percentage rate in such a manner as to consistently understate the annual percentage rate; or (3) otherwise fails to comply with certain other requirements imposed under the TILA. 15 U.S.C. § 1611.

With respect to depository institution deposit activities, the federal regulatory agencies charged with supervising and monitoring depository institutions have promulgated comprehensive regulations prohibiting inaccurate or misleading representations in connection with deposit solicitations, including apparently deposit solicitations involving telemarketing activities. See, e.g., 12 C.F.R. §§ 217.6 and 329.3.

Other depository institution activities that could involve telemarketing also are regulated by specific federal statute. For example, the Electronic Fund Transfer Act, ("EFTA"), 15 U.S.C. § 1693 et seq., sets forth the requirements with which a depository institution must comply in connection with electronic fund transfers, including presumably the sale of electronic fund transfer services, such as debit cards and point of sale cards, via telemarketing. The federal regulations promulgated pursuant to the EFTA establish requirements for the entire range of activities conducted in connection with electronic fund transfers, including the issuance to customers contacted by telemarketing of access devices used to effect electronic fund transfers. 12 C.F.R. Part 205. The EFTA provides for a private cause of action and other penalties comparable to those provided under the TILA discussed above.

Depository institutions also are subject to general prohibitions against fraudulent activities. In this regard, the Federal Trade Commission Act ("FTC Act") prohibitions against engaging in unfair or deceptive acts or practices are applicable to depository institutions pursuant to the provisions of 15 U.S.C. § 57a(f). Specifically, the FTC Act prohibitions against unfair or deceptive acts or practices can be applied to any activity of a depository institution. Id. Thus, the FTC Act supplements the specific prohibitions against fraudulent and deceptive acts and practices contained in the TILA, the EFTA and other federal statutes and regulations.

The federal criminal provisions governing fraud generally and wire fraud specifically, 18 U.S.C. §§ 1341 and 1343, further supplement the specific prohibitions against fraudulent and deceptive activities. As amended by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. 101-73, 103 Stat. 183 (August 9, 1989) ("FIRREA"), these two antifraud provisions both contain enhanced penalties for fraudulent activity that "affects" an insured financial institution -- criminal fines of up to $1,000,000 and/or a prison term of up to twenty years, Id., and civil fines up to the lesser of $1,000,000 per day or $5,000,000. 12 U.S.C. § 1833a. These provisions may be interpreted to include enhanced penalties when the financial institution is a participant in the crime, as well as when it is a victim.

Even more specifically, the federal regulatory agencies may exercise direct authority over marketing and advertising by depository institutions. The OTS, for example, is specifically authorized to regulate "any sale, plan or practices, or any advertising" of state and federal thrifts. 12 U.S.C. § 1468a. In the exercise of this authority, the OTS has promulgated, among other more specific rules, a regulation prohibiting the use by state thrifts and federal thrifts of any advertising or promotional materials (presumably including telemarketing promotions) "which is inaccurate in any particular or which in any way misrepresents its services, contracts, investments, or financial conditions." 12 C.F.R. 563.27(b)(1).

Moreover, depository institutions, as a general matter, are prohibited from engaging in unsafe and unsound practices. In certain circumstances, fraudulent activities can be deemed to constitute unsafe and unsound practices. See, e.g., FRB Interpretation, 1 F.R.R.S. ¶ 3-411 (Oct. 13, 1965).

As is discussed in greater detail below, the federal agencies charged with regulating and supervising depository institutions have extremely broad authority to enforce any law applicable to a depository institution. 12 U.S.C. §§ 1464 and 1818. For example, Section 8 of the Federal Deposit Insurance Act ("FDIA") empowers the federal regulators to remove management officials and employees of a depository institution and issue cease and desist orders against a depository institution for, among other things, a violation of any law (including, presumably any state law), rule or regulation applicable to the depository institution. 12 U.S.C. § 1818. Moreover, the FDIC may terminate the insurance of a depository institution that engages in such violations. Id. The U.S. Supreme Court has recognized that the authority to terminate the insurance of a bank is a "formidable power." See United States v. Philadelphia National Bank, 374 U.S. 321, 329 (1963). "Such involuntary termination severs the bank's membership in the [Federal Reserve System] if it is a state bank, and throws it into receivership if it is a national bank. . . . As a result of the existence of this panoply of sanctions, recommendations by the agencies concerning banking practices tend to be followed by bankers without the necessity of formal compliance proceedings." Id.

In view of the foregoing we believe that the existing statutory and regulatory framework applicable to depository institutions is more than adequate to address any fraudulent activities, including telemarketing fraud, engaged in, or perpetrated by, such depository institutions. Accordingly, it is unnecessary and inappropriate to subject these depository institutions to the provisions of S. 1441 or S. 2494. To do so would impose unnecessary costs and regulatory burdens without any corresponding real benefit to consumers.

The Activities Of Depository Institutions Are Restricted By The Statute Under Which They Are Chartered And Their Chartering Regulator.

In addition to the various prohibitions against fraudulent conduct discussed above, the activities of depository institutions are otherwise pervasively regulated. This "cradle to grave" regulation of depository institutions frequently involves a host of federal and state laws and regulations, depending upon the nature or the type of institution involved.

A depository institution only may engage in those activities permitted under the statute under which it is chartered, as authorized by the regulator granting its charter. A subsidiary or affiliate of a depository institution similarly only may engage in activities specifically permitted for such entities under applicable laws and regulations.

National banks, for example, may engage in only those activities authorized under the National Bank Act ("NBA") and other applicable federal law, as determined by the Office of the Comptroller of the Currency ("OCC"). Section 24 of the NBA, for example, enumerates specific activities permissible for national banks. 12 U.S.C. § 24. These activities generally are limited to those constituting the business of banking and other incidental activities, including discounting and negotiating evidences of debt, loaning money and receiving deposits. *Id.* If an activity is not authorized by the NBA or other federal law, that activity is *ultra vires*, and not permissible for a national bank. For example, with limited exceptions, the NBA (and other federal law) does not authorize national banks to pledge securities for private deposits and, accordingly, such pledging by a national bank has been found to be *ultra vires* and void. *See, e.g.*, *Texas & Pacific Railway Co.* v. *Pottorff*, 291 U.S. 245 (1934).

The activities of subsidiaries of national banks, so-called "operating subsidiaries," also are limited, and are restricted to those activities that are permissible for the national bank parent of the operating subsidiary. 12 C.F.R. § 5.34. In addition, a national bank may not establish, acquire or perform new activities in an operating subsidiary without first notifying the OCC. Moreover, the FDIC, pursuant to its authority as the insurer of the deposits held by national banks, has promulgated a body of regulations addressing the activities of FDIC-insured institutions, including national banks. See 12 C.F.R. Parts 303-353.

The activities of state banks similarly are limited to the activities authorized for such banks under state law, as determined by the state banking regulator. Although such state law varies from state to state, it generally is similar to, or based upon, the NBA. In addition, virtually all state banks must be insured by the FDIC and, as such, are subject to the FDIC's restrictions on the activities of FDIC-insured banks discussed above.

In addition, the activities of federal thrifts chartered by the Office of Thrift Supervision ("OTS") (for purposes of this memorandum, federal thrifts include savings banks chartered by the OTS) are restricted to those permitted by the Home Owners' Loan Act ("HOLA"). See 12 U.S.C. § 1461 et seq. Thus, a federal thrift may not engage in any activity unless that activity is authorized under HOLA. Moreover, a service corporation subsidiary of a federal thrift may not engage in any activity unless the activity has been approved by regulation of, or pursuant to an application filed with, the OTS. 12 C.F.R. § 545.74. Indeed, any time a thrift (federal- or state-chartered) seeks to engage in any new activity through a service corporation, it must provide 30 days prior notice to both the OTS and the FDIC. 12 C.F.R. § 563.37(c). Like national and state banks, federal thrifts also are subject to the extensive body of regulations promulgated by the FDIC as the insurer of thrift deposits after FIRREA.

State thrifts are limited to the activities authorized for such entities under applicable state law, as applied by the state regulator. In addition, pursuant to Section 222 of FIRREA, a state thrift may not engage as a principal in any activity not permissible for a federal thrift without the approval of the FDIC, and generally may not engage even in activities permissible for a federal thrift in an amount beyond the authority of a federal thrift without the approval of the FDIC. 12 U.S.C. § 1831e. Of course, state thrifts, like national and state banks and federal thrifts, also are subject to the regulations promulgated by the FDIC as insurer of the deposits of almost all thrifts.

Affiliates of banks are regulated under the Bank Holding Company Act of 1956 ("BHCA"), as applied by the FRB. Specifically, the BHCA sets forth the restrictions applicable to bank holding companies and their nonbank subsidiaries. The term "bank holding company" is defined by the BHCA as "any company which has control over any bank . . . ." 12 U.S.C. § 1841(a)(1). Pursuant to Section 3 of the BHCA, a company may not become a bank holding company without the prior approval of the FRB. 12 U.S.C. § 1842. In addition, Section 4 of the BHCA provides that, once a company becomes a bank holding company, it may not acquire direct or indirect ownership or control of any nonbanking company, or engage in any nonbanking activity directly or through a nonbank subsidiary of the bank holding company, without regulatory authorization from, or the prior approval of, the FRB. 12 U.S.C. § 1843. The FRB has promulgated regulations listing approximately twenty-four activities permissible for bank holding companies and their nonbanking subsidiaries. 12 C.F.R. § 225.25(b).

The HOLA similarly limits the activities that may be conducted by an affiliate of a thrift. 12 U.S.C. § 1467a. The HOLA generally restricts the activities of thrift affiliates to the activities enumerated in the HOLA, the activities which were authorized by regulation as of March 5, 1987 and, subject to prohibitions or limitations adopted by the OTS (by regulation), the nonbanking activities which the FRB determines to be permissible (by regulation) for bank holding companies (i.e., the approximately twenty-four activities listed in 12 C.F.R. § 225.25(b) discussed above). 12 U.S.C. §§ 1467a(c)(1) and (2); cf. 12 U.S.C. § 1467a(c)(3) (provides less onerous activities limitations for "unitary" savings and loan holding companies than are applicable to savings and loan holding companies generally under the HOLA). Moreover, since the enactment of FIRREA, thrift affiliates have been forbidden from commencing nonbanking activities approved by the FRB for bank holding companies without prior approval of the OTS. 12 U.S.C. § 1467a(c)(4).

Financial Institutions Are Subject To Extensive Regulation And Close Supervision By Bank Regulatory Agencies.

In addition to the general restrictions on the activities of depository institutions and their subsidiaries and affiliates discussed above, each such entity is subject to the regulations of, and supervision and examination by, the OCC, OTS, FRB or state banking authority, and/or the

FDIC (collectively referred to herein as "bank regulatory agencies").

The OCC, for example, is charged "with the execution of all laws of the United States relating to the organization, operation, regulation and supervision of national banks . . . ." 12 C.F.R. § 1.1. Pursuant to this omnibus authority, the OCC generally may regulate the manner in which any national bank activity must be conducted. See 12 C.F.R. §§ 1.1-35.8. For example, OCC regulations establish restrictions on activities ranging from the establishment of security devices and procedures, 12 C.F.R. §§ 21.0-21.7, to lending activities in areas having special flood hazards. 12 C.F.R. §§ 22.0-22.5. In addition, OCC regulations require a national bank and its affiliates to report to the OCC extensive financial and other data on a regular basis. See, e.g., 12 C.F.R. §§ 4.11 and 21.5(a).

Moreover, all national banks generally must be examined by the OCC twice in each calendar year. 12 C.F.R. § 4.11(a). During these examinations, the OCC also may examine any affiliate of the national bank. Id.

In addition, as discussed above, Section 8 of the FDIA provides broad enforcement powers to the OCC, OTS, FDIC and FRB. Pursuant to those powers, the OCC may take the following action with respect to a national bank:

(1) Issue a temporary or permanent cease-and-desist order against any national bank or any director, officer, employee, controlling stockholder, or agent of the bank, any other person participating in the conduct of the affairs of the bank, or certain independent contractors of the bank (including an attorney, appraiser, or accountant) to stop or prevent: unsafe or unsound practices in connection with the business of the bank, or violations of any law, rule, or regulation, or any condition imposed in writing by the OCC in connection with the granting of any application or other request by the bank or any written agreement entered into with the OCC. 12 U.S.C. §§ 1818(b) and (c). "Unsafe or unsound practices" includes the entering by an insured depository institution of a contract with a person to provide goods or services to the institution if the contract would "adversely affect the safety or soundness of the institution." 12 U.S.C. § 1831g.

(2) Remove from office or prohibit from further participation in the conduct of the affairs of the bank any director or officer of the bank or other person described in paragraph (1) above who, under circumstances involving personal dishonesty or willful or continuing disregard for the safety or soundness of the bank, has: violated a law, rule, regulation, final cease and desist order, written condition imposed by the OCC in connection with the granting of any application or other request by the bank, or any written agreement entered into with the OCC; engaged in any unsafe or unsound practice in connection with the bank; or committed any act, omission, or practice that constitutes a breach of fiduciary duty, any of which has caused or will probably cause substantial financial loss or other damage to the bank, could seriously prejudice the interests of its depositors, or by reason of which the director or officer has received financial gain. 12 U.S.C. § 1818(e). Any person removed or suspended from office or prohibited from participating in the conduct of the affairs of a bank as described above or in paragraph (3) below also is prohibited from holding any office in, or participating in the conduct of the affairs of, any other insured depository institution. 12 U.S.C. § 1818(e)(7).

(3) Suspend from office, or prohibit from further participation in the conduct of the affairs of the bank, any director or officer of the bank or other person described in paragraph (1) who is charged in any information, indictment or complaint with committing or participating in a crime involving dishonesty or breach of trust which is punishable under state or federal law by imprisonment for a term exceeding one year. 12 U.S.C. § 1818(g).

(4) Impose civil penalties of up to $5,000 per day upon any national bank which, or person listed in paragraph (1) above who, violates any law, regulation, written condition imposed by the OCC in connection with the granting of any application or other request by the bank, any written agreement entered into with the OCC, or the terms of a temporary or final cease and desist order issued pursuant to 12 U.S.C. § 1818. 12 U.S.C. § 1818(i)(2)(A).

(5) Impose civil penalties of up to $25,000 per day upon any national bank which, or person listed in paragraph (1) above who, commits any violation described in paragraph (4) above, recklessly engages in any unsafe or unsound banking practice, or breaches any fiduciary duty, which violation, practice or breach is part of a pattern of misconduct, causes or is likely to cause more than a minimal loss to the bank, or results in a pecuniary gain to the party. 12 U.S.C. § 1818(i)(2)(B).

(6) Impose civil penalties up to $1,000,000 upon any person described in paragraph (1) above who, and up to the lesser of $1,000,000 or one percent of the institution's assets upon any national bank which, knowingly commits any of the violations described in paragraph (5) above, and thereby knowingly or recklessly causes a substantial loss to the institution or substantial pecuniary gain to such party. 12 U.S.C. §§ 1818(i)(2)(C) and (D).

In addition, any director, officer or other person who, pursuant to an outstanding and effective cease and desist order, has been removed from office or prohibited from participating in the conduct of the affairs of a national bank may be subject to criminal penalties, including fines of up to $1,000,000 and/or imprisonment for up to five years if, among other things, that director, officer or person subsequently participates in the conduct of the affairs of the bank, or without the prior approval of the OCC, votes for a director, or serves or acts as a director, officer or employee of any bank. 12 U.S.C. § 1818(j). Similarly, a person who has been convicted of a crime involving dishonesty or breach of trust may not participate, directly or indirectly, in the affairs of an insured depository institution, and may be subject to the same criminal penalties described in the preceding sentence for violating this prohibition. 12 U.S.C. § 1829.

The FDIC also may institute an enforcement proceeding against a national bank under the FDIA to terminate the insurance of a national bank if the national bank or its directors or trustees have engaged or are engaging in unsafe or unsound practices in conducting the business of the bank; violated any applicable law, rule, regulation or order, or any condition imposed by the FDIC in writing on the bank; or violated the terms of any written agreement entered into with the FDIC. 12 U.S.C. § 1818(a).

State banks also are subject to extensive regulation by the banking department of the state in which they are chartered, as well as by the FRB or FDIC. State banks that elect to be members of the Federal Reserve System are regulated by the FRB. 12 C.F.R. § 208.6. State banks that do not elect to be members of the Federal Reserve System are regulated by the FDIC. See 12 U.S.C. § 1811 et seq.

State member banks and their affiliates are subject to examinations by, and the reporting requirements of, the FRB. 12 U.S.C. § 483; 12 C.F.R. § 208.10. In addition, the FDIC may undertake a special examination of any state member bank whenever, in the judgment of the FDIC, such special examination is necessary to determine the condition of the bank for insurance purposes. 12 U.S.C. § 1820(b).

State nonmember banks must disclose to the FDIC certain financial and other information on a regular basis. See, e.g., 12 U.S.C. § 1817(a). In addition, state nonmember banks are subject to examination by the FDIC. 12 U.S.C. § 1820(b).

Moreover, under the FDIA, both the FRB and the FDIC have the same enforcement authority with respect to state member banks and state nonmember banks, respectively, that the OCC has as discussed above with respect to national banks. 12 U.S.C. § 1818.

Federal thrifts are subject to pervasive regulation by the OTS and FDIC. State thrifts similarly are subject to comprehensive regulation by the OTS and FDIC, and in addition are subject to extensive regulation by state regulators in the state in which they are chartered. All thrifts, both state and federal, are subject to the examination and reporting requirements of the OTS. See, e.g., 12 U.S.C. §§ 1464(d) and (v); 1817(a)(3). In addition, both state and federal thrifts must make certain reports to the FDIC, and are subject to special FDIC examination, if, in the judgment of the FDIC, such an examination is necessary to determine the condition of the thrift for insurance purposes. 12 U.S.C. §§ 1817(c), 1820(b)(3). The FDIC also has the same enforcement authority under the FDIA vis-a-vis state and federal thrifts as the OCC does with respect to national banks. 12 U.S.C. § 1818.

As discussed above, bank affiliates (i.e., bank holding companies and their nonbank subsidiaries) are subject to the regulation of the FRB. Pursuant to that regulation, a bank holding company must register with the

FRB within 180 days after becoming a bank holding company, and must provide, in the manner and form prescribed by the FRB, an annual report of the bank holding company's operations for the fiscal year in which it becomes a bank holding company and for each fiscal year during which it remains a bank holding company. 12 C.F.R. § 225.5. In addition, the FRB may examine or inspect any bank holding company and each of the bank holding company's subsidiaries. 12 C.F.R § 225.5(c). Moreover, under the FDIA, the FRB may issue cease and desist orders and/or impose civil money penalties for violations of the BHCA and the FRB's regulations promulgated thereunder. 12 U.S.C. § 1818; 12 C.F.R. § 225.6.

Additional penalties for violation of the BHCA are provided in the BHCA itself. 12 U.S.C. § 1847. A knowing violation of the BHCA by any individual or company, and a knowing violation by a company of any regulation or order issued pursuant thereto, is subject to a criminal fine of up to $100,000 per day and/or a prison term of up to one year. Additional civil penalties may be imposed on both companies and individuals in an amount up to $25,000 per day. Whoever knowingly violates the BHCA with the intent to deceive, defraud, or profit significantly may be imprisoned for up to five years and/or subject to a criminal fine of up to $1,000,000.

A savings and loan holding company must register with the OTS within 90 days after becoming a savings and loan holding company. 12 U.S.C. § 1467a(b)(1). In addition, a savings and loan holding company, and its subsidiaries, are subject to examination by the OTS and must report to the OTS such reports as may be required by the OTS. 12 U.S.C. §§ 1467a(b)(2) and (4).

The OTS is empowered to initiate an action in federal district court to enjoin any act or practice that constitutes, or will constitute, a violation of the savings association holding company provisions of the HOLA or any rule, regulation or order issued thereunder. 12 U.S.C. § 1467a(g)(4). Moreover, the OTS may order a savings and loan holding company or any of its subsidiaries to terminate any activity that, among other things, constitutes a serious risk to the financial safety, soundness, or stability of the savings and loan holding company's subsidiary insured institution or to terminate its ownership or control of any noninsured subsidiary engaging in such activities. 12 U.S.C. § 1467a(g)(5)(A) and (p). Any savings and loan holding company that violates the holding company provisions of the HOLA, or any rule or regulation promulgated thereunder, may be fined up to $100,000 for each day the violation continues. 12 U.S.C. § 1467a(i)(1)(A). In addition, an individual found guilty of such a violation of the HOLA may may be fined up to $100,000 and/or imprisoned for up to 1 year. Id. If such violation is perpetrated with the intent to deceive, to defraud, or to profit significantly from such violation, the perpetrator may be fined up to $1,000,000 per day and/or imprisoned for up to five years. 12 U.S.C. § 1467a(i)(1)(B). Any company which violates, and any person who participates in a violation of, the holding company provisions of HOLA or any regulation or order issued pursuant thereto also may be liable for a civil penalty of up to $25,000 per day. 12 U.S.C. § 1467a(i)(2)(A).

Conclusion.

MasterCard and VISA believe that it is clearly not necessary to subject regulated depository institutions, and their affiliates and subsidiaries, to additional federal antifraud legislation related to telemarketing in view of the comprehensive statutory and regulatory scheme governing the activities, including the telemarketing activities, of such entities. As discussed above, numerous federal statutes and regulations address the manner in which such entities must offer specific products, such as loan and deposit products, including through telemarketing, and provide for substantial penalties for failure to comply with such statutes and regulations, as well as private rights of action. In addition, regulated depository institutions and their affiliates and subsidiaries may engage only in the specific activities for which they are authorized by applicable statute and regulation. Finally, the bank regulators' supervisory responsibilities and general enforcement powers, as well as the remedies provided in the statutes and regulations governing the offering by telemarketing of specific depository institution products and services, ensure that any fraudulent or inappropriate telemarketing activities of depository institutions, or their affiliates or subsidiaries, are already effectively addressed.

Comments of
the National Consumers League

The National Consumers League appreciates this opportunity to submit comments for the record of the May 2, 1990 hearing regarding S 1441 and S 2494. As a national membership organization, the League is involved in research, education and advocacy on behalf of consumers regarding a variety of issues. Telemarketing fraud, life care communities and long-term care are three of those issues.

National Legislation Needed to Prevent Telefraud

American consumers need national legislation to address the problem of fraud conducted over the telephone. This need is demonstrated by the hurdles consumers must clear in order to successfully pursue a complaint against a suspected con artist. First, consumers must figure out which consumer protection office to contact: their own, or an office in the state where the con artist is located. Virtually all of the telemarketing fraud complaints the League receives from consumers concern a telephone transaction that crosses state lines. Second, once consumers contact these consumer protection offices, they find out that little can be done to enforce the laws of one state in another state. Third, if telefraud victims contact a federal agency like the Federal Trade Commission, or the Securities and Exchange Commission or Commodity Futures Trading Commission in cases of investment fraud, they find that those agencies usually cannot help them either. Lastly, if after pursuing all of these avenues consumers decide to take private legal action, they are faced with tracking down a con artist who likely lives halfway across the country, and instituting a suit in another state. Meanwhile, consumers are losing between $1 billion annually, according to the

FTC, and $10 billion annually, according to the North American Securities Administrators Association.

Definition of Telemarketing

The League is concerned that the definition of telemarketing included in S 2494 is unnecessarily limited by the terms "significant use" and "interstate voice." "Significant use" is an ambiguous term that places an unreasonable burden on an individual or government agency to prove when telemarketing has actually taken place. What is the purpose of the phrase "interstate voice" telephone calls in S 2494? Both S 1441 and HR 1354 do a better job of defining telemarketing. However, the League is concerned that S 1441 is limited to the completion of a sale over the telephone. As we pointed out in testimony regarding HR 1354, completing or consummating a sale over the telephone seems to include only credit card transactions while excluding an agreement to purchase by cash or check. The definition should include payment by credit card, cash or check. Comparing S 2494 and HR 1354, the League would like to see the telemarketing definition apply to a plan, program or campaign "designed or conducted," using the term from each bill.

Telemarketing Rules

The "Rebuttable Presumption" language of S 1441 is favorable to consumers. However, S 1441 is too restrictive in its direction to the FTC regarding a rulemaking on telemarketing, specifically in Section 5(b)(2). On the other hand, the language in S 2494 is broad enough that Section 3(a) should read: "shall include" instead of "shall consider the inclusion of." The League supports the prohibition placed on computer-generated calls included in S 2494. We recommended in testimony regarding HR 1354 that such a prohibition be included in legislation. We would also like to see Senate legislation pick up on the language of the "Prohibited Conduct" section of HR 1354. Finally, the NCL agrees with the provision in S 1441 directing the FTC to extend the Mail Order Merchandise Rule to cover telemarketing transactions. The League commented in January, 1990 to the FTC in support of its proposed rulemaking now under consideration to amend the Mail Order Rule to cover telephone transactions.

State Action

The League believes the general intent of Section 4 of S 2494 is an improvement over the approach taken by S 1441 regarding the authority of state attorneys general to pursue action against an alleged fraudulent telemarketer. State officials should be able to act on their own as opposed to being appointed by the FTC to assist in enforcement. Likewise, the approach of S 2494's Section 4(a)(3) in requiring states to notify the FTC upon instituting a civil action is preferable to the 30-day notice impedement of HR 1354. Unfortunately, in Section 4(a)(7), S 2494 appears to severely limit the ability of the attorneys general and other state officials to go after telefraud in their own states. The League sees no reason why state officials should be required to notify the FTC of an intent to bring action under state law in state court. Furthermore, the FTC should not be able to remove such an action to a district court. The language in this section is overly broad, ambiguous and goes against the idea that state officials should play an integral role in bringing enforcement action against telefraud operators.

Considering the limited ability of the FTC to tackle the numerous telefraud complaints throughout the United States, the rationale of telemarketing fraud prevention legislation should be to enhance the ability of state officials to tackle telefraud. Consequently, S 2494 should not in Section 4(a)(1) limit state action in federal district court to enforcement of FTC rules, regulations and orders. In addition, Section 4(a)(5) of S 2494 should ensure that not only attorneys general, but also other state and local officials be able to exercise their authority under state law. Finally, the term "antifraud statute" in Section 4(a)(6) is unnecessarily broad, and should be clarified by simultaneous use of the phrase "unfair and deceptive acts and practices."

Actions Brought by Private Persons

The League believes that private right of action is an important option that should be available for consumers pursuing redress. S 1441 includes no provision for such action, and S 2494 seemingly excludes individuals from being able to bring suit, while allowing "member organizations comprised of financial institution members..." to do so. Section 5(a) needs to specify, as is done in HR 1354, that individuals also have a right to bring private actions against alleged fraudulent telemarketers in federal district court. In doing this, S 2494 should eliminate the $50,000 minimum amount in controversy for individual private actions. At the least, S 2494 should specifically allow for class action suits. Moreover, precedents for authorizing class actions in consumer oriented laws can be found in the Equal Credit Opportunity Act and the Electronic Fund Transfer Act. These acts as well as the Fair Debt Collection Practices Act, the Fair Credit Reporting Act, and the Truth-in-Lending Act all provide that an action may be brought in federal district court by an individual without a minimum amount in controversy.

The League disagrees with the provision in Section 5(b)(3) of S 2494 that requires a plaintiff in a private action to notify the FTC of the action and allows the FTC to intervene in the suit.

The nature of a particular law suit, the extent of loss incurred, the chances for successful recovery, the disdain for protracted legal battles, and the costs associated with bringing an action, litigating the matter and recovering damages, all serve to limit the number of suits that individuals file. Furthermore, the "Limitation" language of S 1441 would provide financial institutions with protection against possible frivilous suits.

While S 1441 is silent regarding types of relief available to fraud victims, S 2494 briefly discusses relief in Section 4(a)(2). The League believes consumers are benefitted by specific mention of types of relief, and we urge an approach like that in HR 1354 that offers a more comprehensive list. Both S 2494 and HR 1354 should include language that makes it clear the types of relief listed are not the only ones available.

Venue, Subpoena, False Advertising and Mail Covers

S 1441 and S 2494 include virtually identical provisions regarding venue and subpoena. The League believes these sections are beneficial because they strengthen FTC authority. S 1441 includes provisions regarding false advertising and mail covers. Again, the League believes these sections are beneficial because they strengthen FTC authority.

Life Care Home Study and Long-Term Health Care Insurance Study

Regarding provisions in S 1441 that call for two separate studies on life care communities and long-term care insurance, the League supports expanding the role of the FTC in monitoring unfair and deceptive acts or practices in these areas. These studies are a step in that direction. However, the League does not want these studies used as a rationale to preclude additional Congressional action in these areas in light of other evidence of fraud or abuses.

Regarding life care communities, the FTC has an obligation to examine the capacity of the states to establish appropriate standards for financial and contractural integrity and soundness, for appropriate disclosures to consumers about finances and all terms and conditions of the contracts, and to provide the requisite enforcement capacity. The financial and contractural arrangements of life care communities are complex, an amalgam of real estate, nutrition, health care and other industries. These mixed marketplace characteristics create a confused regulatory environment that should be carefully scrutinized by the FTC to assure that consumers are adequately protected against financial failure or deceptive practices in the industry.

The League believes S 1441 should go further than a study and include a provision requiring life care contracts to designate life care community residents and those who have invested to become residents in a community, as secured or priority creditors in the event that the community they have invested in goes bankrupt. We do not need a study to tell us that residents of life care communities should have a reasonable chance to recover some of their life income if the community declares bankruptcy.

Regarding long-term health care insurance, the League is concerned that the definition of long-term care is unnecessarily limited. Current long-term care insurance policies provide benefits for adult day care, home care, respite care and other types of long-term care services. To limit the definition in S 1441 to policies that pay "a predetermined or fixed benefit payment for each day the policyholder stays in a nursing or care facility" does not recognize the universe of what is considered long-term care.

Conclusion

The National Consumers League considers a national legislative approach to the problem of telefraud essential to address the fact that this fraud so easily crosses state lines. As demonstrated in these comments, we find positive and negative provisions in both S 1441 and S 2494. Overall, the League prefers the approach of HR 1354; however, we would like to see any industry exemption eliminated. These three bills certainly provide the Congress and concerned parties the opportunity to forge a compromise bill that would provide consumers with important rights and protections when doing business over the telephone. We look forward to working with the Congress in passing pro-consumer, telefraud prevention legislation and addressing health fraud and abuses.

○

31-349 (192)